DELAYED FUNDS AVAILABILITY

HEARING

BEFORE THE

SUBCOMMITTEE ON CONSUMER AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

TO EXAMINE THE EXTENT TO WHICH DEPOSITORY INSTITUTIONS IMPOSE LENGTHY HOLDS ON CUSTOMER CHECK DEPOSITS, THE REASONS FOR THE GREAT DISPARITY IN THE HOLD POLICIES OF DEPOSITORY INSTITUTIONS, AND ALTERNATIVES FOR SHORTENING HOLD PERIODS WITHOUT INCREASING RISK OF LOSS FROM BAD CHECKS

MARCH 10, 1982

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DELAYED FUNDS AVAILABILITY

WEDNESDAY, MARCH 10, 1982

U.S. SENATE,
SUBCOMMITTEE ON CONSUMER AFFAIRS,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, D.C.

The subcommittee met at 9:30 a.m. in room 5302, Dirksen Senate, Office Building, Senator John H. Chafee (chairman of the subcommittee) presiding.

Present: Senators Chafee and Dodd.

OPENING STATEMENT OF SENATOR CHAFEE

Senator CHAFEE. Good morning. I have called this hearing to examine the extent to which depository institutions impose lengthy holds on customer check deposits, the reasons for the great disparity in the hold policies of depository institutions, and alternatives for shortening hold periods without increasing risk of loss from bad checks.

There certainly are legitimate reasons for placing holds on check deposits. An institution might understandably want to hold a check until it has itself received credit for the funds. It might also impose a hold to protect itself against risk of loss. What concerns me, however, are those institutions that across the board deny customers the use of funds far beyond the time it takes for the bank to receive credit for the check, and without regard to the size of the check, the quality of the relationship with the customer or any other factors that would indicate there was little risk the bank could be stuck with a bad check.

Once a bank has itself received credit for a check deposit, usually with 1 to 3 days, any further hold means the bank is making money market rates on the customer's deposit, while the customer is denied the use of his or her money. In a period of high interest rates, this practice is especially lucrative for banking institutions, and costly for the customers. When the hold is routinely extended, without indication of particular risk, this practice, at best, becomes a hidden cost of checking and, at worst, a genuine consumer abuse.

A recent survey authorized by the Federal Reserve Board indicated 20 percent of the consumers have experienced delayed funds problems. Federal Reserve Governor J. Charles Partee recently stated that in working with various consumer groups and State attorneys general, delayed funds is an issue that "comes right to the top as an area that is most complained about." Federal Reserve Governor Nancy Teeters has stated that next to monetary policy, she is asked most about check holds. For several years, the Federal

Reserve has reportedly been looking at this problem, yet a Fed/ABA task force report and a bank administration institute report and recommendations were not pursued by the Federal Reserve. Thus, there is no Fed policy on this matter, and no effort has been made to officially encourage shorter holds. The Federal Reserve has not even enforced its own wire notification rules.

The Federal Home Loan Bank Board, I might add, declined our invitation even to submit written testimony on this subject for the record.

Invariably, in my conversations about this hearing, I heard personal horror stories. I have heard of banks that won't let their customers use the check deposit, nor let them dip into their line of credit because it was the held check that gave the customer a positive, though unusable, balance. I've heard of a bank that only holds checks in increments of $100 and so held $70 of already cleared funds on a $30 deposit. And we all have our own horror stories. I think everybody here in this room has them and certainly I have personal horror stories.

Now there is an acknowledged problem out there, but there is no data on it, and nothing has been done about it.

My staff and Senator Dodd's staff conducted our own random telephone survey of banks, S. & L.'s, and credit unions in the Washington area, New York, Connecticut, and Rhode Island. Our purpose was simply to get a sampling of the range of check hold periods. We found a wide disparity in the treatment of check deposits, with some holding local checks as long as 10 business days. That's 2 weeks. A New York savings bank we called held New Jersey checks, even certified checks, for 14 business days, which seems impossible, yet that is what the customer relations officer told us. I must say I'm looking forward to some testimony of why in the world do you have to hold a certified check. What is a certified check if it isn't a genuine verifiable amount of cash that is in deposit in the bank in one's home town or in the issuing bank?

One Virginia savings and loan holds Maryland and D.C. checks as much as 15 business days. That's intolerable. That's 3 weeks. And other out-of-town checks 21 business days—1 full month—with no exceptions. We also found that in a great many of the institutions followup calls produced widely inconsistent information. This raises the question of how well informed employees are of their own policies and ultimately the quality of the information available to customers.

On the other hand, we also found many institutions have hold policies that are very generous to their customers. I seriously question why, if these institutions can maintain such policies without undue losses, others cannot as well.

In view of the history of regulatory inattention to a recognized consumer abuse, I believe it is time the Congress took a good look at this problem.

If new regulations by the Federal Reserve System and other regulatory agencies, or legislation by Congress, are not needed to correct the problem, then I believe the burden now lies with the industries and regulators to show why. I look forward to the testimony we will receive this morning.

I might say that I start off with a bias against further regulation. I don't want to do it. I don't believe in it wherever it's possible to avoid it, but I certainly think we are dealing with an area where there are genuine abuses and if we are not to have further regulation or laws on the subject, then what's the alternative, and I look forward to hearing suggestions along those lines from the witnesses.

Our first witness is Theodore E. Allison, Staff Director for Federal Reserve Bank Activities of the Board of Governors of the Federal Reserve System. Mr. Allison, we welcome you here and look forward to your testimony.

STATEMENT OF THEODORE E. ALLISON, STAFF DIRECTOR FOR FEDERAL RESERVE BANK ACTIVITIES, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

Mr. Allison. Thank you very much, Mr. Chairman.

I, too, believe we can avoid regulation in this area. I look forward to discussing that with you.

[Complete statement follows:]

Statement by

Theodore E. Allison
Staff Director
for Federal Reserve Bank Activities
Board of Governors of the Federal Reserve System

I am pleased to have the opportunity to present the views of the Board of Governors of the Federal Reserve System regarding delayed funds availability policies and practices. Delayed funds availability is a practice employed by some banks, savings and loan associations, credit unions, other depository institutions, and non-depository institutions such as money market mutual funds whereby the depositor of a check may not withdraw the funds represented by the check for some period of time to assure that funds are available in the depositor's account if the check is returned unpaid. When confronted with problems involving these policies, many depositors are understandably irritated; often they must delay other transactions, and some may even realize costs as a result.

Today I would like to explain briefly how the check collection system works and how it relates to delayed funds availability; to share with you what the Board has learned from its studies of delayed availability problems and practices; and to explain what, in the Board's view, would be the most productive approach in seeking solutions to the problems that exist.

The Check Collection System

The check collection system in the United States frequently involves many handlings of a check between its deposit in one depository institution and its payment by the paying depository institution. Checks deposited to accounts in the same institution at which they are to be paid account for about 51 percent of all checks written. The remaining 49 percent of the checks must be collected by sending them (as shown in Diagram 1) to:

- a correspondent bank;[1]
- a Federal Reserve office;[2]
- a check clearinghouse;[3]
- the paying depository institution directly; or
- some combination of the above (the most likely alternative).

As little as one day or as many as six or more days may be required for a check to move from the institution at which it is first deposited (the endorsing institution) to the paying institution. The actual time required depends on the number of intermediary institutions involved, the weather, distance, whether there are holidays or weekends involved, and the exposure to mechanical breakdowns in transportation or sorting equipment, and potential human error. Upon receipt of the check, the paying institution deducts funds equal to the amount of the check from the balance in the maker's account, if the check is properly drawn and endorsed, funds are available, and there is no stop payment order. But if the check is not properly drawn, not properly endorsed, if funds are not available, or if there is a stop payment order, then it will send the check back to the endorsing institution. (See Diagram 2 and Table 1.) When a paying institution returns a check, it must do so by midnight of the day after it receives the check.

Article 4 of the Uniform Commercial Code, which has been adopted in all states, governs check clearing and requires the paying institution to return the check to the institution from which it received the check. Thus, if several institutions were involved sequentially in the clearing process, each institution must also handle the check as it is returned to the depositor. Although the processing of return items is the reverse of the original processing for collection, this process is much more labor intensive. The machine readable coding at the bottom of the check allows for collection routing through the use of computer controlled high speed check sorters. A check being returned, however, must be processed manually because each endorsement stamp on the back of the check must be read to determine the institution to which the check should be returned. As a result, return routing might typically require twice as much time as collection routing. For example, a check requiring two days to be delivered to the paying institution might require four additional days to be returned to the institution of first deposit. Unfortunately, at the time a check is first deposited, there is no way of knowing whether it will be paid or returned unpaid.

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[1] A correspondent bank is any depository institution that provides services and holds balances for other depository institutions.

[2] Federal Reserve Banks process approximately 40 percent of all checks written.

[3] A check clearinghouse is usually an association of depository institutions which may serve many needs of its member institutions including the exchange or clearing of checks.

Slightly more than 1 percent of all checks the Federal Reserve collects--about one-half million checks per day--are returned unpaid. (See Table 1 for details regarding returned checks handled by the Federal Reserve.) We believe that return experience is similar for the checks not collected through the Federal Reserve.

Correspondent institutions and the Federal Reserve grant credit for checks that they collect for depository institutions using an availability schedule which reflects the normal processing and transportation time involved. For example, if a Federal Reserve office is normally able to collect a check in one day, it gives one day availability. Most commonly, the Federal Reserve provides credit within two days. However, reflecting the uncertainty regarding a check's being paid or returned, the credit granted is provisional, and the institution receiving the credit must be prepared to give it up immediately should the check be returned unpaid. Likewise, depository institutions' depositors must also be prepared to make restitution of any funds credited to their account should a deposited check be returned unpaid, even though a delay in availability may have been imposed.

There are several alternatives to the use of checks that can ensure against the problems and risks associated with checks returned unpaid. Many payments--especially those that recur regularly such as salary, dividends, and social security--can be received through automated clearing houses, and others can be handled as wire transfers. Both of these electronic means of payment are secure against loss or theft, and entail immediate and (usually) irrevocable credit to the receiver's account. I will discuss these alternatives in more detail later.

Delayed Funds Availability

Delayed funds availability is one way that institutions may protect themselves from the risks involved in the event a check is returned unpaid by the paying institution to the institution in which it was first deposited.

Delayed funds availability is practiced by all types of depository institutions but varies widely among individual institutions. A study done by Federal banking agencies in 1978 found that 38 percent of the commercial banks surveyed had adopted some formal delayed funds availability policy, often specifying widely different procedures and criteria. Some institutions rarely or never delay availability. Frequently, institutions tailor the delay by considering their own exposure to individual risk--how well known the depositor is to the bank, the amount of the check, the average time required for collection and return of unpaid checks between this institution and the paying institution, and so forth. In other cases, institutions apparently delay funds on all checks or all out-of-town checks.

Whether the delay is imposed selectively or not, delayed funds availability is often characterized as "unfair" to depositors. Institutions, however, defend the practice as a means of protecting themselves from losses associated with returned checks. As the previous description of the check collection system shows, there is no mechanism for informing an endorsing institution affirmatively that a check has been paid. One way for an institution to avoid loss in the event a check is returned unpaid is to delay the depositor's use of the funds. The longer the delay the less risk that the check might be returned and loss incurred by the institution. Thus, in view of the check collection system in this country, selective delayed availability policies and practices have a legitimate business basis and may contribute to the safety and soundness of depository institutions.

It is frequently charged that delayed funds availability practices are intended to generate increased revenues for depository institutions at the expense of depositors. It may well be that certain institutions are able to enhance their revenue through the practice of imposing blanket rather than selective delay policies. This would be true since blanket delay programs are relatively easy to implement and affect all or most checks deposited. However, a selective delayed availability policy may entail considerable expense for the institution, since training employees to identify the need for and length of delay is costly, and selectively imposed delays are handled as exceptions to routine procedures. Moreover, delayed availability policies are just one of a number of terms and conditions--including service levels, check fees, required balances, hours of operation, location of branches, and interest rates--which must be considered as a whole in determining the costs and benefits of the account relationship for the customer. Thus, a less selective policy, such as imposing a delay on all out-of-area checks deposited, which would seemingly be more profitable for the institution, might be used in conjunction with lower fees or lower minimum balance requirements than would otherwise be the case. In effect, a less costly, less selective policy could be part of a product preferred by customers who are more interested in low fees and low minimum balances than a short delay in using their funds.

The Federal Reserve has made an effort to keep informed of delayed availability practices and problems, both because of its role in the monitoring of consumer complaints about banking practices and because of its reponsibility for the effectiveness of the payments system. For example, we have a formal procedure for receiving, tabulating, and investigating consumer complaints involving banks. In the last five years the number of complaints involving delays in getting the use of funds has consistently been only about 1 or 2 percent of the total number of consumer complaints. (See Table 2.)

In addition, the Board has sponsored three surveys of consumers' problems with delays in use of funds deposited by check in their accounts--one in 1977 and two in 1981--all conducted by the University of Michigan's Survey Research Center. Twelve hundred account holders were queried in the two most recent surveys. Ninety percent had rarely or never experienced delays over the past few years. Less than four percent had experienced frequent problems. The same question was asked in the 1977 survey, and indications are that a slight increase in consumers' problems has occurred during the intervening period. One possible explanation for this may be the higher level of interest rates recently, which may have provided incentives for banks to be more cautious in making funds available and for depositors to maintain lower checking and savings account balances.

Of the four percent of all respondents who reported problems, the consequence of delayed funds availability for about one-fifth was having checks they had written on their accounts returned, which probably led to personal distress and possibly to the levy of a service charge as well. By contrast, four-fifths of the consumers experiencing problems said their problem involved inconvenient delays in purchasing goods, in getting cash, or some other sorts of inconvenience. More often than not, consumers indicated that the inconvenience had not been serious.

The cause of the delayed availability problem mentioned most frequently by consumers was lack of awareness of the bank's policy--either they never were informed of the policy or they had forgotten it. Of those depositors who experienced problems, substantially more than half appear to have contacted their depository institution and believed that the institution was helpful. The 1978 bank survey found that 97 percent of the banks which had a delayed funds availability policy also had an officer authorized to make exceptions to the policy.

In addition, the consumer surveys indicated that depositors know a variety of ways to avoid problems once they become aware of the practice and that those who have had the most problems are most likely to have changed their habits or practices to avoid further problems. For example, many said they would plan ahead, keep enough money in their account, carry more cash, or cash their checks elsewhere and then deposit the balance not needed right away. When asked what they would do if they thought they would have to wait at least four days to use their money, the most frequent response was that they would change depository institutions. Consequently, depositors who are better informed apparently can and do take steps to avoid future problems and are better equipped to bring competitive forces to bear when policies are judged unreasonable.

What Should Be Done?

The Board is sympathetic to the problems that depositors face as a result of delayed availability policies, especially when delays appear long relative to normal check-collection-time requirements and when problems are the result of consumer unawareness of the policies. It believes that two approaches warrant further attention. First, the Federal Reserve System will expand its efforts to investigate possible ways to speed up the handling of returned checks. If substantial progress can be made in this area, depository institutions that impose delayed availability could reduce the length of the delays. In this connection, the Board has also directed that a study be conducted to determine whether existing Federal Reserve services can be enhanced or new Federal Reserve services developed to achieve prompt final settlement of certain types of checks that seem to cause delayed availability problems more frequently. These might include large payments for deposit in another part of the country--such as for the purchase of a house--or periodic payments by parents to students attending school away from home.

Second, the Board believes that financial institutions should on their own initiative better inform their depositors of the extent and nature of the delayed availability policies and practices that they employ. Improved consumer awareness is needed on this subject. Our surveys show that depositors who know to ask often get some accommodation in particular cases from an official of their institution, generally avoid problems thereafter, and are prepared to change institutions if necessary when confronted by what they consider an unreasonable funds availability policy. In this connection, the Federal Reserve and the American Bankers Association have agreed to reinstate a joint task force on delayed availability practices to address among other things the issue of disclosure by banks of their funds availability policies. The recommendations developed through this joint effort will be made available to other interested parties, including other supervisory agencies and other depository institution trade associations.

The Board does not believe that it would be advisable to adopt a legislative or regulatory approach to this practice. To attempt to define, through legislation or regulation, an "appropriate" maximum delay period would be difficult or impossible given the complexity of our nation's check collection process. Any such legislative or regulatory maximum could well become the industry standard, thus worsening the situation for the majority of customers and reducing the efficiency of the payment system. Moreover, under any legislative or regulatory approach, if the risk of loss could not be avoided by selectively delaying funds availability beyond some maximum, fees or required balances would probably be increased by depository institutions to fund anticipated or actual losses.

Meanwhile, the Board will continue to monitor carefully the complaints it receives on this issue, and it will periodically conduct further University of Michigan surveys.

Finally, the Board wishes to note some alternatives to receiving payments by check that depository institutions and their customers can use to avoid the need for or the effects of delayed funds availability. Recurring check payments such as salary, dividends, social security, and so forth, can most efficiently be accomplished through the automated clearing house (ACH). The ACH is a form of electronic funds transfer that does not have the delays associated with check collection.

More infrequent, large dollar value transactions, such as the transfer of the proceeds from the sale of a former residence to a depository institution in a new location, are suitable for wire transfer, a service designed to accomplish large dollar payments in a secure, rapid, and irrevocable manner.

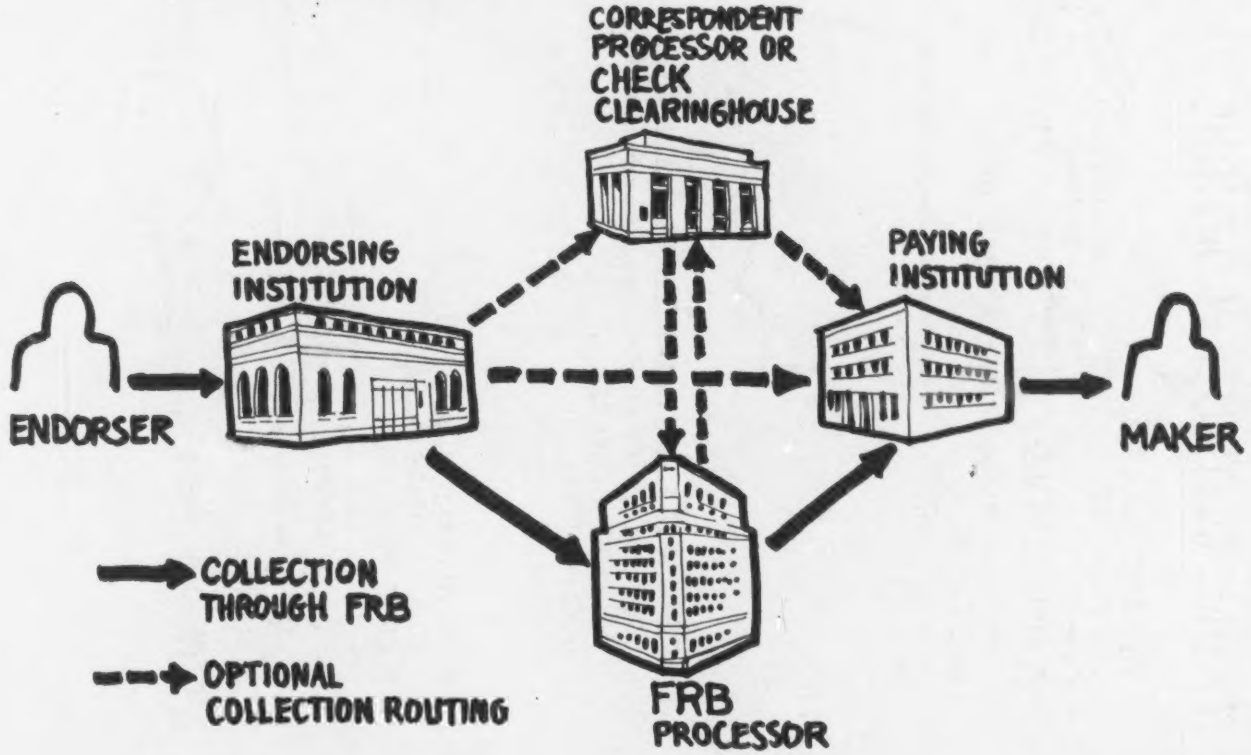
A depositor having a large dollar value check and wishing to use a check collection method that includes an affirmative notice of payment or non-payment may use the "non-cash collection" service, which functions in the following manner. Upon instructions from its depositor, a depository institution may send a collection letter to the paying institution, enclosing the check and specifying that funds in payment of the check are to be wired to the originating institution for deposit to its depositor's account. Funds will not be credited to the depositor's account until received. Moreover, the preparation of the letter at the sending institution and processing at the paying institution are manual processes, the cost is substantially higher than the regular check collection cost, and five to ten business days may be required for completion of the transaction. Nonetheless, this may be a desirable alternative to assure that the check will not be returned since transaction is final once the paying institution has sent funds. In this manner, the depositor can invest or spend the funds when received without concern that the check may be returned subsequently.

Conclusion

Consumers have experienced difficulties with the funds availability policies and practices of some depository institutions, and the Board and the Reserve Banks are moving on two fronts to help find ways of improving the situation. They are undertaking a study of possible improvements in check collection procedures that would achieve faster handling of return items or faster confirmation of payment or nonpayment of checks; and they will be working with the American Bankers Association on ways that depository institutions might improve customer awareness of their funds availability policies. The Board does not believe that delayed availability problems are sufficiently widespread that Federal legislation or regulation would be desirable at this time. The Board will, of course, continue to monitor consumer problems and attitudes in this area.

DIAGRAM 1

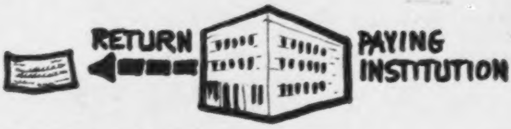
CASH ITEMS


CORRESPONDENT PROCESSOR OR CHECK CLEARINGHOUSE
ENDORSING INSTITUTION
PAYING INSTITUTION
ENDORSER
MAKER
FRB PROCESSOR
COLLECTION THROUGH FRB
OPTIONAL COLLECTION ROUTING

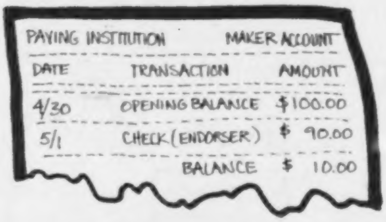
PAYING INSTITUTION OPTIONS

DIAGRAM 2

1. AUTOMATIC RETURN-
STOP PAYMENT
FRAUD
ACCOUNT CLOSED...


RETURN
PAYING INSTITUTION

2. SUFFICIENT FUNDS IN MAKER'S ACCOUNT-
DEBIT MAKER'S
ACCOUNT AND
PAY ITEM

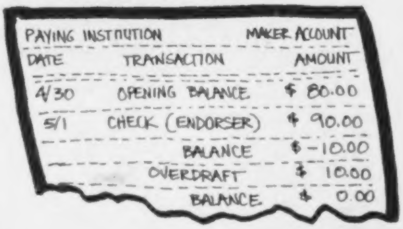


PAYING INSTITUTION MAKER ACCOUNT

DATE	TRANSACTION	AMOUNT
4/30	OPENING BALANCE	$100.00
5/1	CHECK (ENDORSER)	$ 90.00
	BALANCE	$ 10.00

3. INSUFFICIENT FUNDS IN MAKER'S ACCOUNT-

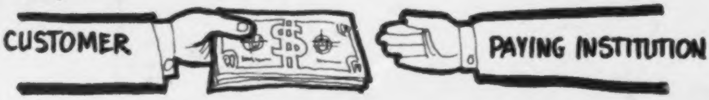
A. APPLY OVERDRAFT LINE
OF CREDIT IF COVERED,
AND PAY ITEM; OR



PAYING INSTITUTION MAKER ACCOUNT

DATE	TRANSACTION	AMOUNT
4/30	OPENING BALANCE	$ 80.00
5/1	CHECK (ENDORSER)	$ 90.00
	BALANCE	$ -10.00
	OVERDRAFT	$ 10.00
	BALANCE	$ 0.00

B. PAY ITEM AND ATTEMPT TO
COLLECT FUNDS FROM
CUSTOMER; OR


CUSTOMER
PAYING INSTITUTION

C. RETURN ITEM

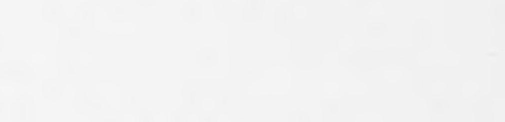

RETURN
PAYING INSTITUTION

Table 1

Maker vs. Reason For Returns
Percent of Total Number of Returned Checks

	REASON FOR RETURN							
Maker	Insufficient Funds	Account Closed	Endorsement Errors	Payment Stopped	Post-Dated	Uncollected Funds	Other	Total
Individual	60	9	2	2	2	1	2	78
Business	12	2	2	3	0	1	1	21
Other	0	0	1	0	0	0	0	1
	72	11	5	5	2	2	3	100

SOURCE: Federal Reserve Bank of Philadelphia, sample of 1,119 return items, September 1981. Findings correspond to similar prior study by Bank Administration Institute.

Table 2

Total Funds Availability Complaints
Received by the Federal Reserve System
1977-1981

	Total Complaints	Funds Availability Complaints	Percent
1977	3,474	45	1
1978	3,301	46	1
1979	4,065	75	2
1980	4,568	95	2
1981	3,913	75	2

Senator **Chafee**. Thank you very much, Mr. Allison.

Senator Dodd is here. Senator, we welcome you and if you have an opening statement this should be a good time for it.

OPENING STATEMENT OF SENATOR DODD

Senator **Dodd**. Thank you, John. I apologize to you, Mr. Allison, for not being here at the outset. I thank you for your statement.

Mr. Chairman, I want to thank you for holding these hearings. In the lexicon of the issues facing the country, I suppose that delayed funds availability may not rank the highest in everybody's mind, but it's certainly an important issue to the industry and to thousands of customers who have had problems with our financial institutions. At any rate, I'm sure we all know people who have suffered frustration, embarrassment as well as a financial penalty when a check they had written bounced because their bank had not yet credited a previously deposited check.

Therefore, I'm glad, Mr. Chairman, as I mentioned earlier, that you called these hearings so we can examine bank policies on check holds and the reasonableness or the unreasonableness of these policies.

We're fortunate to have a report from the Fed on delayed funds availability that provides, I believe, a good starting point for our examination. This study concludes that placing holds on customers' checks is a widely employed technique. The main purpose of placing holds appears to be to protect banks against the problem of collecting on returned items. In fact, they appear to have been very successful at this.

In 1973, a bank industry study found that less than 1 percent of all checks processed are returned. In 1973 the estimated losses from uncollected funds was a total of $5 million. Now in 10 years I presume that's at least doubled. It may even be tripled, but even so, in terms of the total amount being handled, that's a small amount.

HOLDING PERIOD

At the same time, the Fed report shows that banks have the opportunity to make significant sums of money while customers are waiting for their checks to clear. This is true because banks get—as you pointed out already, Mr. Allison, in your testimony—provisional credit for checks 1 to 3 days after they are entered for collection. They can then invest those funds, I presume, until they credit the checks to their customers' accounts which is some time later. Clearly, the value of even 1 day's float must vastly exceed the amount of moneys lost, whether that be $5 million, $10 million, $15 million, or whatever the figure is today, and I'm not sure we have that figure but based on the 1973 study.

A joint staff survey by this committee confirms that banks do make money while placing holds on customers' checks. Our staff has surveyed the hold practices of more than 50 financial institutions in the metropolitan areas of Washington, D.C.; Hartford and New Haven, Connecticut; as well as various cities in Rhode Island, and they found most banks will not credit a personal check drawn on a local bank for 3 to 4 working days and on an out-of-state bank for more than 10 days. This hold period provides them with a long time during which they can earn money on the float while, too often, their customers sink.

In light of the very limited size of their losses, I think there's a heavy burden on the financial institutions that will appear before us today to justify their hold policies.

Finally, if the facts are as they appear to be, I would hope, Mr. Chairman, that we could all work together to devise a system that provides a better balance between the legitimate needs of the banks to protect themselves against uncollectable checks and the equally legitimate needs of their customers for prompt access to their funds.

Mr. Chairman, I'm looking forward to the rest of the testimony and I appreciate again the opportunity to have these hearings.

Senator CHAFEE. Well, thank you, Senator, for that fine statement, and I share with you the concern that when this affects an individual it really affects an individual quite severely. It's an embarrassment. It's a delay. It's a frustration. I noticed in some of the testimony we have before us it discusses tuition checks mailed—I guess this was in a news article—tuition checks mailed to or funds mailed to children who were away attending school and the checks don't clear and there's a great difficulty ensuing even though your statistics show it to be a very modest amount.

I notice you cited the Michigan survey, Mr. Allison, and I looked at that and my review of that shows that in 1977 the percentage of those having problems with delayed funds availability was 12 percent. In August 1981, it was 17 percent; and in November 1981, 3 months later, it was 23 percent of those surveyed. I'm not sure quite where you got your statistics that it's only 1 percent.

Mr. ALLISON. My figures, Mr. Chairman, were 4 percent, I believe, and I was referring to those with frequent problems.

Senator CHAFEE. With frequent problems.

Mr. ALLISON. Yes. We asked the respondents—or the University of Michigan survey asked the respondents to characterize their problems as either frequent, sometimes, hardly ever, or never.

Senator CHAFEE. Well, it's the old story. It's like having appendicitis. It may not be frequent, but when you have it it's difficult and it hurts.

So I think to base your statistics solely on frequent is a trifle misleading in this area.

Mr. ALLISON. The combination of persons with frequent problems, sometimes problems, and hardly ever problems might run closer to the number you mentioned.

Senator CHAFEE. And also mentioned by your Gov. Nancy Teeters, who said as I mentioned in my opening statement that next to monetary policy she's asked most about check holds. She's pretty close to the Federal Reserve I assume.

Mr. ALLISON. Surely.

Senator CHAFEE. Now you mentioned that the Federal Reserve Board is concerned about the problem with delayed funds and, as I understand it, this was first identified as a problem in 1976 and then there have been—in 1979, the BAI released its recommendations—since all this started, it's been 6 years, and now you say you're going to study the problem again.

I just wonder how seriously you take this issue and why has it taken so long and how long can we expect before something specific is recommended.

Mr. **Allison**. Mr. Chairman, it's been a difficult issue. We have tried to gather objective data. We have, as I indicated, a consumer complaint process. We have made an effort to sample customers. We do make a distinction between those that have hardly ever had problems and those who have more frequent problems. Our indications are time and again from the sources we have looked at objectively that the problem is not widespread. It does not seem to be locally concentrated either in local areas, although it perhaps is more customarily found in metropolitan areas than nonmetropolitan areas; but aside from that generalization, it is not a localized problem either. It's a difficult problem to deal with also because it doesn't lend itself to regulation. We have a complex check clearing process in this country.

WIRE SERVICE NOTIFICATION SYSTEM

Senator **Chafee**. Well, in your testimony you didn't mention at all the wire service notification system that you have of checks that have bounced, yet that's available and not only is it available, as I understand it, but it's included in the fee that is already paid to the Fed.

Could you describe a bit about that and why did you happen to exclude it? It seems to me it's a fairly important service that you didn't even mention in your testimony.

Mr. **Allison**. Yes. Our operating circulars governing our own check collection operations in the Federal Reserve Banks provide that any financial institution returning a check which it originally received from the Federal Reserve must, if the check is in the amount of $2,500 or more, initiate a wire advice which will be forwarded by the Federal Reserve to the financial institution from which it received the check. It should be noted that regulation J and the related operating circulars of the Reserve banks apply only to checks that are collected by the Federal Reserve—only about 22 percent of all checks written.

We have proposed to make our operating circular requirements more effective, Mr. Chairman, and are in the final stages of that regulatory procedure now. We have proposed to make these requirements more effective by imposing on returning banks a warranty that they in fact did make that wire notice and a requirement that they indemnify any sending bank of costs involved as a result of their not having made the wire notification as required.

So we believe that this provision of the operating circular as it has existed hasn't been attractive to institutions and it hasn't been much used. We think we have——

Senator **Chafee**. I didn't quite understand. What hasn't been much used?

Mr. **Allison**. The wire advice—the wire advice concurrent with returning the check. For one thing, it's specified in the Federal Reserve operating circulars. It's not customarily an agreement among private institutions clearing checks among themselves. In a sense, it therefore imposes a double kind of operating procedure on banks.

They must remember that if they are returning a check to the Federal Reserve they must initiate a wire advice at the same time they return the check. If they are returning that check to the private collection system they need not do so. That obviously imposes operating costs on the institution and so it hasn't been very widely used.

Senator **Chafee**. Imposes operating cost on what institution?

Mr. **Allison**. On the paying institution returning the check, for initiation of that wire advice.

Senator **Chafee**. But if the institution is sending the wire is with the Federal Reserve, they are paying that—that service is covered anyway by the costs that are imposed on them for the handling of the check. Isn't that true?

Mr. **Allison**. We don't make a separate charge for handling returned items. The item is returned by the paying bank, the bank to which the check was presented. It's the depositing bank who pays, in effect, for our check-collection service. So there really isn't a charge in any event on the paying bank but there is operating expense. What's necessary is for there to be an incentive for the paying bank in fact to make that wire notification at the time it elects to return the check rather than to pay it. There needs to be an incentive.

What we have proposed to impose upon the bank is a warranty that in fact it did make the required wire notification and as well as a warranty to impose the requirement that it indemnify any institution within the stream, including the depositing bank, or indemnify those organizations from any loss as a result of its not providing that wire notification. We think that will be effective.

Senator **Chafee**. What have you done about that?

Mr. **Allison**. We've proposed that for comment and have received and analyzed the comments. It was one of a package of items that were designed to improve our check-collection services. It's in the final process now of staff analysis. We expect it will be presented to the Board reasonably shortly. And, while I can't speak for the Board, Mr. Chairman, I rather imagine it will be approved. I do believe it will be an enhancement.

Senator **Chafee**. Not enough of an enhancement for you to even mention it in your testimony, though.

Mr. **Allison**. Well, it's included in those items that I indicated would speed up the handling of returned items and would provide faster notification of the payment or nonpayment of a check. I meant to cover this point in those last closing remarks, Mr. Chairman.

What's really needed here is less certainty for the depositing bank, the collecting bank—less certainty as to whether the check has been paid or not. That's really the key to shortening the delay time.

Senator **Chafee**. Less uncertainty you mean, don't you?

Mr. **Allison**. I'm sorry. More certainty, less uncertainty.

Senator **Chafee**. My time is up. Senator Dodd.

Senator **Dodd**. Thank you.

Let me pick out a couple things if I can. You're familiar with the 1979 Fed/ABA task force and you pointed out, I think quite correctly, it would be unfair to require banks to give customers the use of funds from a deposited check until the bank receives provisional credit for the check. I think all of us understand that. There are some risks involved. The effect of the immediate credit policy, as pointed out in the study, would be an interest-free loan to the customer.

MONETARY VALUES OF HOLDING POLICY

However, once the bank has received provisional credit for the check, I believe that we've got to balance the risk of loss from uncollected checks against the money that a lending institution makes on the float before the customer can use his or her money, and I'd like to take a look at the 1979 study and then your testimony as well.

In the 1978 survey which you referred to in your testimony, you pointed out that some 38 percent of the banks said that they had formal hold policies on checks and that, I guess, by inference, means that 62 percent generally do not have a hold policy, based on your testimony; is that correct?

Mr. ALLISON. The 62 percent at that time apparently didn't have a formal policy. They probably did selectively apply holds.

Senator DODD. Now in the 1979 study and that was on page 4 of your testimony citing the 38 percent, I will quote from the 1979 study. It says:

> Based on the Board's survey finding that about half the banks surveyed have formal policies establishing delays on all or certain checks received in deposits and the observations of banker task force members that banks without formal policies probably practice delayed funds availability in certain cases, the task force concluded that delayed funds availability is widely employed and common banking practice.

How can you in your statement rely on a 1978 study when a year later suggest that roughly 50 percent—and let's not use widely to mean more than 50 percent but take the sentence that about half of the banks surveyed—how does that disparity occur?

Mr. ALLISON. Well, I wasn't implying any disparity. I wouldn't suggest at all that even a larger number of banks than 50 percent wouldn't on occasion, when presented with a certain factual situation, delay availability of a check, Mr. Dodd. I was only indicating that 38 percent at that point did not have a formal delayed funds availability policy.

Senator DODD. Had a formal policy.

Mr. ALLISON. Thirty-eight percent had a formal policy. More than half did not have a formal policy at that time. That relates to the desirability of requiring a disclosure.

Senator DODD. I don't want to quibble about it being 38 percent or 50 percent. Let's use your figures.

Looking at your survey, appendix A, the percentage of banks that gave depositors credit for personal checks drawn on banks in the same city for 4 or more days—so taking your chart A, personal accounts, same city, 4 or more days, and totaling the percentages from 4 to 6, 7 to 9, and 10 to 12, 13 or more days, I come up with a total of 31.5 percent.

Do you have any disagreement with that figure?

Mr. ALLISON. No. I'm sorry. I don't have those right in front of me, but I'm generally familiar with the tables.

Senator **Dodd**. So that clearly, based on your own testimony, these banks make money on the float on 3 to 12 days worth of interest, if the banks generally receive provisional credit within 1 day, which is what your testimony is.

Mr. **Allison**. They generally receive provisional credit within 1 or 2 days, yes.

Senator **Dodd**. But we're finding 31 percent of them—the same city personal checks are 31 percent do not credit the depositor for 4 or more days. With respect to personal checks written out of State, the vast majority of banks did not credit deposit accounts for at least 7 days, and if we just do the out of State we'll find that totals 68 percent. So if it normally takes 2 to 3 days for the bank to get provisional credit, these banks are also making money on the float.

I'm wondering why you didn't have in your testimony some estimate of how much the banks make on the float? While we do have estimates on the losses from uncollected funds, which total in the 1973 study about $5 million a year, you don't have any estimate on the amount made on the float; is that correct?

Mr. **Allison**. Well, that's really an impossible thing to say. After all, the essence of banking is taking deposits and lending that money out.

Senator **Dodd**. It's impossible to determine that figure?

Mr. **Allison**. Well, you would have to make some assumptions about what would happen to those deposits if it were not for the hold. As I indicate, the vast majority of customers appear not to have had a problem. One might assume that the vast majority of customers would have left those funds in the account in any event, whether there was a hold placed on them or not. Those are the essential assumptions that have to be made in citing what the profitability of the hold policy is.

Senator **Dodd**. Let me ask you this. The 1973 study says $5 million of losses. Do you have any more recent figures than the $5 million?

Mr. **Allison**. No. I would only comment that the loss figures are in the context of banks employing a delayed funds availability policy, so it would not be surprising to see low loss figures.

Senator **Dodd**. If we said it was double in 10 years, you wouldn't disagree with that figure?

Mr. **Allison**. I have no way of knowing what it might be. I really don't.

Senator **Dodd**. Let's use the 1973 figure of $5 million total losses in a year from all banking activities as the figure. I'm willing to accept it's double. I'll even accept triple that figure 10 years later for whatever reason. Let's say it's $10 million a year that banking institutions lose as a result of uncollectable checks. What I tried to do was figure out then how much banks are apt to make on the float, in other words, in dealing with this problem by using delayed funds availability.

Let me run through what I went through and I want you to tell me where you think my assumption is unfounded for one reason or another. OK?

$1 BILLION A DAY

Now the average daily amount advanced by the Fed to banks in 1981 was $2.788 billion, and the Fed handles 40 percent of all checks. Those are your figures, the Fed figures. Now private banks, obviously, process 60 percent of the checks. If their activity is 60 percent, then you come up with an average daily balance amount advanced by the Fed and the banks of about $7 billion, taking the Fed's $2.7 billion and the other 60 percent totals the $7 billion, and if we multiply that figure by the average rate for a 3-month Treasury bill of 14.03 percent, then we can estimate the value of 1 day's float as around $1 billion, roughly. Exactly, it comes out to be $977 million, but roughly $1 billion would be the value of 1 day's float.

Now we know that the banks get credit from the Fed or the private system generally in 1 or 2 days, again depending on how far the bank is that the check is drawn upon. Clearly, there's some period of time between when the bank gets provisional credit for the deposit of funds and when it permits the bank's customer to use the money.

If we use highly conservative figures based on in-State and out-of-State checks of 3 days, then we would get a figure of some $3 billion in that 3-day period using your average daily float, and then over 3 days based on the provisional credit, you come out with $3 billion. Now using your figure of 38 percent rather than 50 percent of the banks that engage in a delayed funds availability or hold practice, then roughly we are dealing with $1 billion, roughly one-third of that $3 billion.

Now whether or not we're talking about $5 million or $10 million or $15 million on yearly losses as a result of uncollectable checks through this process as against approximately—unless you can tell me that I've made some egregious error in my formulation of a policy to determine that—against $1 billion in moneys made by lending institutions on the float, that's a heck of a price to pay for a policy that is questionable by your own accounts.

Where have I gone wrong?

Mr. ALLISON. Senator, let me just mention a couple things. First, the vast majority of deposits in checking accounts in this country are commercial accounts, the great majority. I wish I knew the number. I don't have it at my fingertips, but the vast majority of the deposits that are made are to commercial accounts, and commercial customers generally have negotiated availability arrangements with their banks. They may get immediate availability but have minimum balance requirements such that any returned checks are able to be covered by the commercial organization or there may be in some other form a delayed availability policy that's negotiated between them. It is, believe me, the vast majority of deposits are to commercial accounts.

So we're talking about deposits to customer accounts which is quite a small proportion of that total volume which you mentioned and, again, on the loss side, I would just emphasize that the loss figures you cited are low—they're in the context of policies designed to avoid those very losses, and this suggests that banks have been——

Senator **Dodd**. How many checking accounts are there in the United States, roughly?

Mr. **Allison**. How many checking accounts? I don't know. I would be happy to try to furnish an estimate for you, though.

Senator **Dodd**. Would it be 50 million?

Mr. **Allison**. Let's say 50 to 100 million.

Senator **Dodd**. Ten percent of the people who have problems quite often or frequently have problems—let's use 75 million—that's over 7 million checking accounts, people having problems. That's not a small item.

Mr. **Allison**. I was including commercial accounts in my estimate, but take a smaller number.

Senator **Dodd**. Savings accounts, they have people with problems. You mentioned that includes everything—savings accounts, money markets, mutual funds—these are all of them.

Mr. **Allison**. By contrast, 90 percent don't. Senator, I'm not suggesting it's not a problem. It is. It is a problem. The question is how best to deal with it.

Senator **Dodd**. Well, you have to agree—and I'll terminate here—that given the recognizable losses $5, $10, $15 million amount that is earned or made through on the float is substantially more than the losses, whether you exclude commercial accounts or not. There's a tremendous disparity there. Would you agree with that?

Mr. **Allison**. I would say, Senator, that policies may very well be lucrative, may very well be in some situations. I wouldn't argue against that for a moment.

Senator **Dodd**. Let me stop here.

Mr. **Allison**. They may not be. They may be costly to implement depending on the nature of the delayed policy. One has to look behind the policy I think.

Senator **Chafee**. Mr. Allison, in your testimony on page 8, the Board has also directed that a study be conducted to determine whether existing so forth can be enhanced. When did you make up your mind to have that study?

Mr. **Allison**. The Board directed that study about 10 days ago.

Senator **Chafee**. After we let you know we were going to have some hearings?

Mr. **Allison**. That's the first consideration in my statement this morning, Mr. Chairman.

TIMETABLE TO EXPEDITE RETURN PROCESS

Senator **Chafee**. Now in New York State it's my understanding that they are introducing legislation in connection to this matter, and what would happen if we just put—a board member, Mrs. Teeters has said, perhaps facetiously, if you put an absolute limit on holds the banks would figure out a way how to expedite the return process. Do you think she was facetious or do you think they would figure out a way to comply?

Mr. **Allison**. It would impose an incentive on the banking industry.

Senator **Chafee**. It certainly would. What's your thoughts on that?

Mr. **Allison**. I think it would probably be detrimental on balance. Mr. Chairman, I believe there are a lot of institutions that do not impose unreasonable delays, that probably impose delays shorter than those that would be specified by law, and I think there's always a certain risk that those customers would be made worse off as a result.

I think there's also the possibility—the real possibility of exposure for banks, exposure to fraud, if they must make checks available on a certain timetable. I'm certain if a collection routing can be worked out that results in a longer time than that for a check to be returned banks would probably be taken advantage of.

Senator **Chafee**. Some suggest that the competitive system can work here, that if you don't like the bank you're dealing with, go elsewhere; but that, to me, is no answer at all. What you're usually dealing with—and I'm not suggesting you're making that answer, but I just want to rebut the suggestion that that is a way of dealing with it—let the competitive system work because what happens in the typical case is that a person goes into the bank—one of the principal reasons the check is held up is that he isn't known and he's not Nelson Rockefeller with his name on the check for depositing it. So that once he gets in there and the delay starts, unbeknownst to him—and the record clearly shows that there's no uniformity of notifying a person—he makes a deposit, goes out—a student is a typical case—his father sends him the check, deposits it and it's meant to pay his tuition and nothing happens. Tick, tick, tick—on goes the time. And for the student then to come in and reverse the whole process—take the check out, try and go elsewhere is really no answer at all.

Mr. **Allison**. The problem with students, of course, is difficult because they are new in the community and so on, but in general, let me just say this about the competitive structure of the banking industry and the likely efficacy of that kind of approach. It doesn't really require the customer to change accounts in order to change institutional behavior. It only requires that they be willing to do so and indicate that to their bank officers. One thing that has surely changed in the last couple years is the competitive structure of the banking industry. There are now 25,000 more institutions able to offer checking accounts than was the case 1½ years ago—all the credit unions, savings and loan associations, mutual savings banks, and so on. They are very much competing for checking account business at this moment.

So I think, Mr. Chairman, that better informed customers, better able to deal with their institutions' check officers, probably would result in changes in their favor.

Senator **Chafee**. Well, we will send the signal out as much as we can to customers to complain when this takes place. Usually the situation is when finally the check clears it's a mixture of anger over the delay and relief that it's finally cleared—like your children coming home late at night—angry that they're late, but so relieved they're home safely.

Now explain to me why a money order—let's take a bank check. Why in the world—let's take the same city on this chart—the same city for a cashier's check to clear in 18 percent of the cases takes—well, let's move up—in 41 percent of the cases, it takes more than zero days. Why is that? What more can you do than to have a cashier's check?

Mr. **Allison**. Mr. Chairman, I'm not here this morning to speak for the banking industry and I hope you also will direct that question directly to the banking industry.

I can speak as someone knowledgeable about the check processing system, the way that checks are handled among banks. Even within a metropolitan area, scenarios can be developed that would take several days for a check to be presented to the paying bank and then returned to the depositing bank.

Senator **Chafee**. We're talking about a cashier's check.

Mr. **Allison**. Making immediately available the funds represented by a cashier's check also entails some risk for the bank. The risk there, as I understand it, is that the person presenting the check is in fact the payee on the check. That is, there's the question whether the check has been forged or stolen and is being fraudulently presented. As I understand it, that's a risk. I hope that you will pursue that question with the representatives of the banking industry.

Senator **Chafee**. I will. I have no further questions. Do you have any more questions?

Senator **Dodd**. Just a few more. Just a couple more if I can. I'd like to just address some of the options that you considered and I might get your views on it. I might point out as well that you suggested another study. As the chairman has pointed out, of course, you had that study in 1979. We kind of study things to death.

RECOMMENDATIONS

You made some recommendations in 1979 and as I read your testimony many of the suggestions that you're making in your testimony today reflect the recommendations of the 1979 study.

Mr. **Allison**. They do.

Senator **Dodd**. And I'm sort of intrigued about why we go back and go through a whole other study again. Basically, I assume you will make the same conclusions.

Mr. **Allison**. Well, this next study shouldn't take very long and if the recommendations are the same——

Senator **Dodd**. Just a carbon copy of the 1979 might do.

Mr. **Allison**. If the composition of that task force has changed a good bit and if that group still sees the problem in the same way and still sees the solutions in the same way, they will be presented to the Board and, I suspect, acted on.

Senator **Chafee**. Could I just interrupt? You considered the last study was acted on? You said presented to the Board and acted on.

Mr. **Allison**. That study wasn't presented to the Board, Mr. Chairman.

Senator **Dodd**. Why not?

Mr. **Allison**. Well, there was a good bit of disagreement on the staff about it. There were some and there continue to be some who question whether this is a widespread enough problem that any kind of Federal supervisory action ought to be taken. The essence of the report was the Federal supervisory action, the issuance of a policy statement by the Board of Governors. That does imply supervisory action.

There are some who question whether the problem is that serious. There are others who question whether that would be an effective step.

Senator DODD. Why don't we save some time? Basically, I think, Mr. Allison, you can tell us this morning that the likelihood that the 1982 study is going to say anything different than the 1979 study is deminimis, correct?

Mr. ALLISON. There are a couple respects in which I would hope the study might go further, the recommendations might go further than they did.

Senator DODD. But in effect, what you're going to be suggesting is in essence that banks maybe do a bit more. As you point out in 1979 in the first two points that they give written notice to customers and let them be aware of these things and so forth, but——

Mr. ALLISON. That's likely to be the essence of the recommendation.

Senator DODD. So basically, going to a study is kind of ridiculous. We know what the Fed is going to recommend, don't we really? There's nothing better to put a number of Congressmen and Senators at ease than to announce that we're going to do a study.

Mr. ALLISON. This one won't take very long.

Senator DODD. OK. Let me just run down a couple of these things. The blanket policy—I think there probably isn't a person in the room that disagrees that it's the blanket policy that is the difficulty. You don't take into consideration the customer, the amount of the check, the point of origin and so forth.

Mr. ALLISON. Right.

Senator DODD. And those are the things that should be taken into consideration, that there should be a more specific policy that banks engage in rather than blanket policies as a whole. Is that correct? Is that your general conclusion?

Mr. ALLISON. Well, my preference as a consumer would be that that be my bank's policy. My preference as a representative of a bank supervisory agency would be that the supervisory agency should not get into the business of prescribing what those policies ought to be.

Senator DODD. But you would certainly recommend it be more specific than general?

Mr. ALLISON. And the customers know what the policies are.

Senator DODD. And to be more specific than general without specifying what the specifics ought to be.

Mr. ALLISON. Well, I'm not certain.

Senator DODD. I'm trying to get you off the hook.

Mr. ALLISON. Well, I think I'd just as soon not be off that hook. The recommendation of the task force study was that the bank adopt a policy and disclose it. If banks adopt policies that are unreasonable and they lose business, well, perhaps they deserve to lose that business.

Senator DODD. It's intriguing, I suppose, that a representative of the Fed won't take that policy but yet the Bank of America will take that policy.

Mr. ALLISON. I took the policy as a consumer.

Senator DODD. How would you feel about requiring banks to establish policies based upon their actual experience? I gather your last statement——

Mr. ALLISON. Well, as a consumer, I think the policy ought to be grounded in fact and in banking practice.

Senator DODD. Why do you have difficulty speaking as a consumer?

Mr. ALLISON. I'm having difficulty speaking as a bank supervisor.

Senator DODD. Isn't our job really to be obviously conscious of the needs of the institution but certainly just as mindful of the needs of the consumer?

Mr. ALLISON. Surely. The question is how to do it. We much prefer that consumers themselves and banks themselves in the marketplace come to those kinds of policies.

Senator DODD. And in fact, in laying out a policy that would disclose to the customer coming in exactly what those policies are?

Mr. ALLISON. Exactly what it is.

Senator DODD. How would you feel about a requirement that banks not hold checks for more than 3 days after they receive provisional credit and accompany that with a requirement that the bank on which the check is drawn notify the paying bank by wire if a check bounces? I think the chairman may have already raised that point.

Mr. ALLISON. That I think must be investigated and we are currently looking at the wire notification issue. The threshold for wire notification, however, would be a rather high dollar amount at this point.

Senator DODD. I was going to suggest $2,500.

Mr. ALLISON. $2,500 to $5,000, yes.

Senator DODD. How about a system of 3-day credit to the depositor and permit banks to charge interest? That's been I think done by some—some lending institutions offer that service where you hedge against the possibility of an uncollectable check.

Mr. ALLISON. Indeed, this whole area involves the creditworthiness of the depositor and if that kind of arrangement could be worked out it might be quite effective.

Senator DODD. I guess you're going to change the front page of that final report and recommendations in 1979 and redate it maybe March 1982. OK. Thanks, Mr. Chairman.

Mr. ALLISON. We will do that promptly and we really are interested in——

Senator DODD. We can do that right back here. [Laughter.]

Thank you, Mr. Chairman.

Senator CHAFEE. Thank you. We look forward to the report, Mr. Allison, and that you send us up a copy of it when it's completed.

Mr. ALLISON. We certainly will, and there will be more than the report. We will also be looking for improvements in the check handling process that can help this situation as well.

[The following information was subsequently received for the record:]

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF THE STAFF DIRECTOR
FOR FEDERAL RESERVE BANK ACTIVITIES

April 8, 1982

The Honorable Christopher J. Dodd
United States Senate
Washington, D. C. 20510

Dear Senator Dodd:

In response to your request at the March 10, 1982, hearings of the Subcommittee on Consumer Affairs on the banking practice of delayed availability of funds, the Board's staff has developed an approach to determining the amount of bank revenues derived from delayed availability. However, while the staff has developed what is, in my view, a thorough and analytically sound approach to calculating such revenues, the actual calculation cannot be performed without considerably more information, much of which would be difficult or impossible to obtain.

Sincerely yours,

Theodore E. Allison
Staff Director

Enclosure

METHODOLOGY FOR CALCULATING INCREMENTAL BANK REVENUES FROM DELAYED AVAILABILITY OF FUNDS ON CHECK DEPOSITS

At the March 10, 1982 hearings before the Subcommittee on Consumer Affairs of the Senate Committee on Banking, Housing, and Urban Affairs, Senator Dodd requested information from Mr. Allison on the amount of bank revenue currently derived from funds for which credit availability is delayed pending possible return of checks deposited.

A formula is developed below that would be appropriate for calculating an approximation of this component of revenues. However, it is not possible to evaluate this formula at the present time, because all of the data needed are not known. In order to make the calculation, it would be necessary to obtain statistical information describing the distribution of the size of checks deposited, by category of depositors and availability of items. Also needed would be the proportion of check deposits to which earnings rates should apply. Data on the required check distributions would be difficult and costly to obtain, because manual inspection would be required of the payee information that is written but not encoded on the face of the checks. The proportions of different kinds of deposits to which earnings rates should apply would require sampling the deposit/withdrawal behavior of bank customers.

Derivation of the Formula

The basic method for calculating revenues from delayed availability involves multiplying the dollar value of check deposits that would have been withdrawn but could not be because credit availability was delayed, times the amount of time that credit was delayed, and then multiplying by the rate of return of the funds to the banks. For checks deposited to noninterest-bearing transaction accounts, this calculation can be represented by the term:

$D\ (1-p)\ T\ I$

where:

D = Average daily value of checks deposited.

p = Proportion of the value of checks (D) to which an earnings rate should not be applied for the present purpose, because the funds would have been left on deposit irrespective of the delayed availability policy. Thus, $(1-p)$ represents the proportion that would have been withdrawn but could not be when there are delays in availability. When there are no delays, $(1-p)$ represents the proportion that is actually withdrawn before it is collected by the bank.

T = Time difference, expressed in days, between credit of the bank customers' deposits, and provisional credit received by the banks.

I = Rate of return banks earn on the funds per annum.

To this term must be added a second term representing revenues from checks deposited to interest-bearing transaction accounts such as NOW accounts, or to interest bearing accounts from which funds are transferred to transaction accounts as they are needed. This second term has the form:

$H\ (1-q)\ T\ (I-r)$

where:

H = Average daily value of checks deposited to interest-bearing accounts to which the interest rate (r) would apply.

q = Proportion of the value of checks (H) that would have been left on deposit irrespective of the availability policy. It is similar to p above.

r = Annual rate of interest that banks pay on the accounts. This would be a composite, or weighted average, rate on the several kinds of interest-bearing transaction accounts and funds in accounts that can readily be moved to transaction accounts.

The formula also needs to take into account the effect of different credit given and received by banks for different kinds of items. Banks receive provisional credit, subject to later reversal if the items are later returned for reasons such as insufficient funds, for various kinds of checks on different days, depending on the location of the institutions on which the items are drawn. When the banks delay availability to their customers, they generally do so based on the number of days typically required for possible return of the items. The time required for return of local checks is less than that required for return of out-of-town items.

For the present purpose, five categories of checks are differentiated. The actual check collection process is considerably more complex than the simple model represented by the five categories of checks represented here. For example, the time of day of a deposit can be a factor in the calculation of credit availability, because it determines whether or not an item is received in time to process and dispatch to another bank for receipt prior to a deadline. Banks pass credit to each other on the basis of schedules of closing hours for particular kinds of items, and late arrival normally means delay of credit by one day. Distributions of arrival times are not known and are not included in the model represented below. Bank size and geographical location are other variables that are important in the check clearing process, but are not included in this model. However, the method used here should be adequate for the level of approximation required for the present application.

Not only does the time difference (T) vary for different categories of checks, but also the proportions of p and q vary because funds from large checks are treated differently by bank customers than funds from more routinely deposited smaller checks. Funds are also managed differently by different kinds of customers.

Combining the terms that were developed for both noninterest-bearing and interest-bearing accounts, and distinguishing between types of items, provides a formula for calculating the net annual revenue (R) to banks from delayed availability of items.

$$R = I \sum_{i=1}^{5} [D_i \; T_i \; (1-p_i)] + (I-r) \sum_{i=1}^{5} [H_i \; T_i(1-q_i)]$$

The subscript i denotes the types of items deposited as follows:

$i = 1$ indicates small local items deposited by consumers and small businesses.

$i = 2$ indicates small out-of-town items deposited by consumers and small businesses.

$i = 3$ indicates large local items deposited by consumers and small businesses.

$i = 4$ indicates large out-of-town items deposited by consumers and small businesses.

$i = 5$ indicates items deposited by large businesses.

Evaluation of the Time Difference Terms

$T_1 = -1$ day

Explanation: Most banks traditionally have given consumer accounts same-day credit for small local checks, even though the items could not be collected until the following day. The size of these accounts has generally been sufficiently large to protect banks against small items that were returned. The time difference is minus one day. The minus sign indicates that such items reduce the earning assets of the bank until they can be collected.

T_2 = -2 days

Explanation: Same as T_1 above, except that most out-of-town items cannot be collected for two days. The time difference is therefore minus two days.

T_3 = +3 days

Explanation: On average, banks give credit to consumers and small businesses for large local items in about four days because this is a typical period of time required for such items to arrive back at the endorsing bank if they are returned. Banks receive provisional credit for such items in about one day. Therefore, the time difference is 4-1, or 3 days.

T_4 = +8 days

Explanation: Same as T_3, except that times for return and receipt of credit are approximately 10 and 2 days, respectively.

T_5 = Not Known

Explanation: The time for crediting deposits of large business firms is frequently negotiated. Thus, the average period of time before credit is granted is unknown.

Comments

1. The revenues formula could be further refined in several ways. For example, elimination of delayed availability could change both bank costs and fees, but these would be secondary effects, and they would be very difficult to estimate.

2. Some factors are not included in the formula because they are imponderables. Without the revenue gained from delayed availability, many banks might find it necessary to amend certain of the services now offered such as free checking, free check blanks, or longer banking hours to either increase revenue or reduce costs associated with the transaction account service. Nevertheless, the formula as shown should provide a usable approximation of revenues if all of the terms could be determined.

3. The formula, as shown, cannot be evaluated for two main reasons. First, the terms D_i and H_i which represent the distribution of delayed availability items are not known, and no information is available from which they can be estimated. Second, measures of p_i and q_i are not available and would be very difficult to estimate even if D_i and H_i were known.

4. Estimating I, and r seems more tractable in the abstract than estimating the other variables. The earnings rates (I) of different classes of institutions differ from each other, and they vary over time, so some weighted average would have to be applied. The average interest rate (r) that banks pay lies in the range from around 5 percent on NOW accounts to close to the Federal funds rate on certain other types of accounts. Determining the weights to use in computing the average is the problem.

5. The fact that T_5, the delay time for business checks, is not known is not a serious problem, because delays faced by consumers and small businesses are the focus of the present interest. The term with T_5 could be eliminated, and the formula would then represent only the incremental bank income from delayed availability for consumers and small businesses.

Division of Federal Reserve Bank Operations
April 1982

Senator Chafee. Thank you, Mr. Allison, for coming up.

Father McEwen, we are working under some time constraints because the Senate will be going into session at 12:30, I believe today, so I think we will have to move along here and would ask that you summarize your statement if you could. We want to thank you for coming down from Boston.

STATEMENT OF FATHER ROBERT J. McEWEN, DEPARTMENT OF ECONOMICS, BOSTON COLLEGE

Father McEwen. Thank you, Mr. Chairman. I will be happy to do that and ask you to submit the whole statement as drafted for the record.

Senator Chafee. Your whole statement will be in the record.

[Complete statement follows:]

STATEMENT OF

ROBERT J. McEWEN, S.J.
Professor, Dept. of Economics, Boston College
Former President, Consumer Federation of America, Inc.

Members of the Committee:

My name is Father Robert J. McEwen. I am a professor in the Department of Economics at Boston College. My background includes service as President of the Consumer Federation of America, twice President of the American Council on Consumer Interests and currently Vice-Chairman of the Conference of Consumer Organizations. All three are National Consumer Groups. In addition to that I have served as President for many years of the Association of Massachusetts Consumers, a State Consumer Organization. Presently, also, I am serving as a member of the Consumer Advisory Council to the Federal Reserve Board.

I congratulate you ladies and gentlemen on this committee for holding these hearings on the delayed availability of funds. While this particular issue may not seem earthshaking in comparison to some of our other economic problems affecting us today, it still is sufficiently onerous on numerous consumers to be worthy of the public attention which you are directing to it today.

SUMMARY

Let me summarize my concern about this issue in the following points:

1. To hold deposited check funds unavailable to the depositor anywhere from one to 20 business days* seems to me to be an unconscionable imposition on the consumer, in this case the depositor. It has no genuine justification in any of the aspects of the financial structure of this country that I have been able to discover.

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*In calendar terms, a ten day "hold" makes a depositor wait 2 weeks and a 20 day "hold" almost equals a month.

2. The system seems to be designed to make it a thousand percent safe for the bank to which the consumer brings his checks to be deposited. The possibility of the bank losing under the present circumstance is practically zero while the inconvenience to the depositor can be either minimal or quite considerable.

3. All the evidence I have seen indicates that clearing process at most takes two days and all the rest of the time now imposed on the consumer is due to relative inefficiency of the banking process in either returning checks to the receiving bank or informing that bank of the unavailability of funds to cover those checks. In the absence of any consumer or governmental pressure to diminish this extraordinary delay imposed on the consumer, I see no hope of correcting this situation.

4. The cases of small, great and even extreme hardship inflicted on consumers are numerous enough in my own experience to warrant some serious congressional attention to this matter because it seems clear that the banking industry on its own will not move to prevent the continuation of these consumer abuses.

SMALL BUSINESS

May I suggest also to this committee that the issue is not merely inconvenience to individual consumers as such, but investigation would also reveal, I believe, considerable inconvenience to small businessmen whose problem of survival in this economy is bad enough as it is without the banking structure adding further difficulties to their lives.

Let me give you one example. A small businessman of my acquaintance in Los Angeles deposited a check from one of his customers, another Los Angeles firm, for roughly twenty-three thousand dollars in a Malibu bank which is about fifty miles north of Los Angeles. That check was drawn also on a large Los Angeles bank. He owed a bill to his supplier on the east coast for twenty thousand and on the strength of that deposit wrote his own check to cover that debt and deposited it in the mail the same day he deposited the Los Angeles check in his Malibu bank. Because the Malibu bank put a hold or a delay on the release of funds from that check, when his own check got to his east coast supplier, it was refused payment by the California bank and he was in the embarrassing position of being called by his suppliers saying your check bounced. Now, in this particular case, the payment of that bill by the day he had mailed his check involved a two percent discount, which was put in jeopardy by this action of the California bank in delaying crediting the account. That small businessman not only was embarrassed in the eyes of his supplier but ran the risk of losing approximately five hundred dollars.

I suggest investigation of other small businessmen's plights would reveal many other cases similar to this.

ILLUSTRATIONS

I have had students in my own classes tell me that, because one of their roommates' checks from their father in a neighboring state had been delayed by the Boston bank, the telephone bill that was paid by that individual became overdue. The telephone company moved in and removed the telephone from the girls' apartment and there was a substantial, as you might imagine, reconnection charge imposed by the telephone company.

PROBLEMS

My overriding concern in this matter is the apparent over-kill practiced on consumers by the banking industry. To the best of my knowledge the loss percentage on checks is well under one percent. Maybe closer to six-tenths of one percent of all checks written turn out to be uncollectible. Then we find the banking industry imposing on the other 99 percent of depositors these unconscionable delays in availability or access to their funds to protect the banking system from the less than 1 percent of the deposited checks that might prove uncollectible. I find it hard to understand how the banking system can justify penalizing 99 percent of the depositors to take care of the possible loss imposed by less than 1 percent of the depositors.

As long as the system remains the way it is, I see little incentive on the part of the banks to be considerate of the inconvenience they are causing depositors.

Another aspect of this situation has to do with the fact that logic seems to have very little to do with this practice because in some of the surveys I have seen, delays are imposed even against checks from the very same city, let alone out of town or out of state.

Another very serious aspect of this whole matter concerns the disclosure of information by banks to potential and actual depositors about their policies in this matter. I have seen one brochure from a California bank that mentions this possible hold on deposited funds but makes it appear to be an extraordinary affair that would not happen very often and would, therefore, not alert the consumer to the reality of the policies of the bank.*

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*Bank of America. *Facts about Bank of America's Checking and Savings Programs. Effective November 1979.*

> HOLDS
>
> The bank may occasionally place a "hold for uncollected funds" for the full amount of a check you deposit if the check is: (1) for a sizable amount; (2) drawn on another bank or branch; or (3) issued by a person or organization whose reliability isn't known. A "hold" means that, although the deposit is immediately credited to your account, you cannot use the funds until the check has cleared (been processed and paid).
>
> Your teller will advise you if a hold is to be placed on your account. (If you make a deposit by mail or through the Instant Deposit box in the branch lobby, you will be notified by return mail.) Your teller can inform you of the number of business days (Saturdays, Sundays, and holidays excluded) the hold will be in effect. If you have any questions, discuss them with the teller when you make the deposit. -- page 31.

I, therefore, suggest that a lot needs to be done to correct the information made available by banks about the policy that a bank will follow in imposing delayed availability on customers.

It appears from the information I have that the problem is greatest in the bigger cities and in the bigger banks where the personal relationship between depositors and the bank personnel is more distant and less personal than in smaller establishments.

I also suggest that this cumbersome and archaic practice is a blot on the banking system of this country and does great damage to the ideal that we have a financial payments system that is universal or nationwide. It almost looks as if the payment system does not function unless you restrict your activity to the one branch bank where you have your main account. This, I think, is running counter to the effort of the banking and financial industry to tell us that we have a unified, integrated, smoothly oiled payment system that can accommodate the needs of both business and individuals throughout the length and breadth of this land.

[I am appending to this statement several pages from students who reported on information given them at local banks with regard to the delayed availability policies. No effort was made to double check this data because it represents information actually given to inquiring consumers.]

The main emphasis of this paper is on the holding period of a deposited check. Holding period here means the elapsed time from the day of deposit to the day your money is available to you. Banks impose holding periods long enough to cover the maximum time it might take the check to clear. Most banks can use your funds within 2 or 3 days but make you wait often as many as 10. The information on this banking procedure is in nearly all cases unavailable to the consumer. The only way to reveal a banks' policy on this subject is to ask, the banks do not print any information because it is only detrimental to themselves. From the banks' point of view there is no need to point out this negative aspect of their procedure in check cashing. However, the prospective bank account opener wishes there was more adequate information available. Most holding periods for respective types of checks are similar at all banks. There is an exception, however. Government checks sometimes require up to a 10 day hold as at Shawmut Savings or no hold at Merchant's Cooperative Bank. It seems as though some banks trust the government while others do not. Research has been done in several areas, 1) The Check Collection system, 2) Laws governing the banks procedure on this matter, 3) from newspapers and periodicals and fourthly, into the consumers feelings and opinions about the delayed availability of their funds due to long and unfair check holding procedures. The data from 9 area banks is compiled in the following table.

SUMMARY

BANK	NO. OF BRANCHES	PERSONAL CHECK (in-state)	PERSONAL CHECK (out-of-state)	GOVERNMENT CHECK
BAYBANK	125	5	10	no hold
BRIGHTON CO-OPERATIVE	2	7	14	7
CHARLESTOWN SAVINGS	14	4	8	8
EDGARTOWN NATIONAL BANK	1	7	14*	no hold
FIRST NATIONAL BANK OF BOSTON	35	3	10	10
MERCHANT'S CO-OPERATIVE BANK	4	5	10	no hold
SHAWMUT SAVINGS	29	3-5	8-10	8-10
UNION WARREN SAVINGS BANK	11	7	up to 21	7
UNITED STATES TRUST	9	3-4	7-12	7-12

ALL DAYS ARE BANKING BUSINESS DAYS
NO BREAKS ON CASHIER'S OR TELLER'S CHECKS
NO PAYMENTS AGAINST UNCOLLECTED FUNDS

*Bank policy requires an additional seven days for checks written on banks west of the Mississippi River

-Table A- Deferred Availability Terms-

Bank	Time (Days)* Min.	Max.	Distance Dependent**	Immediate Old Customer	cash Delivery $ to Back Check	Type of Check
Bank of N.E.	3	10	✓	✓	no exc. -	No
Citizens Savings	2-3	10(20)	✓	✓	✓	No
Durfee Attleboro	2	16	✓	no exception -	no exc. -	No
F.R. Five Cents	5-7	10	✓	✓	✓	No
F.R. People's C6-op.	7	21	✓	✓	✓	Gov't
F.R. Savings	3	14	✓	✓	✓	No
F.R. Trust	2	16	✓	no exc -	no exc -	No
Lafayette	-	10		✓	✓	No
Union Savings	5	14	✓	✓	✓	No

* business days

** time depends on distance check has to travel

A third student submitted the following results:

BANK	HOLD POLICY	
	Same City	Out-of-town
Baybank	3-5	9-10
State Street	1	10 plus
Provident	4-5	
Mutual Bank	5	6-7
Brookline Savings	5-6	10-12
Capitol	2-4	6-10
Coolidge Corner Co-op	3-5	10
First National	2-3	10 plus
Five Cent Savings	5	10
First American	2-4	8 plus
Commonwealth	4	8-10
Elliot Savings	2-4	8-10

UNREASONABLE DELAY ON THE CONSUMER

Father McEwen. I try to make the issues general in this statement. What I think is at stake here, as you gentlemen have mentioned, is that the banking industry in this matter is being put in the position of imposing an unconscionable delay, an unreasonable delay on the consumer. I congratulate you for your scheduling of these hearings because the education of the public about this matter is one of the most important things that will result from hearings such as this.

I think that if we cannot get the Fed to declare this an unfair banking practice—to make an unreasonable delay in making funds available—we shall be left with nothing more than confrontation between consumers and the banking industry. I have pleaded with the banking industry leaders in these statements to try to be sensible about it and don't go the way of the automobile industry. It stonewalled all consumer suggestions for years until they are now falling on their faces. I suggested in a meeting in Washington last winter that there's a correlation between the amount of consumer attention paid by an industry and its problems and distress. The automobile industry paid very little attention in the earlier days of the consumer movement to consumer complaints and I think there's a correlation between their present condition and their absence of consumer input.

I suggest to you that you have been hitting on something that's important and that is that this system is designed to make it 1,000 percent safe for the bank. They can't lose under this system where they don't give you access until they get the money. The banking industry is supposed to be a risk-taking industry and it looks as if they've made sure there's no risk at all in this process.

As you have said, and all the evidence I have seen indicates, the clearing process takes at the most 2 days. For your record I will give you a reference and a quote from the very latest study of this matter put out by the Atlanta Fed called "A Quantitative Description of the Check Collection System," and it's referred to as the Atlanta Fed study. On page 4 of that study I will read you just this quote:

> The best condition estimate of average speed of collection was 1.9 days. Given the way the Nation's banks use the check collection system and assuming optimal processing and transportation conditions, 80 percent of the 125.6 million commercial checks deposited on an average day in 1979 could have been paid by the following day. Based on the check flow model, the best case estimate of the average time from deposit to payment was 1.9 days.

So I see no possibility outside of enlightened action on the banking industry's part, which I'm waiting to see—I see no possibility of correcting this situation unless consumer and governmental pressure is put on them and on the industry.

CONGRESSIONAL ATTENTION

The cases, as I think you have indicated, of small and even great hardship inflicted on some consumers are numerous enough, in my judgment, in my experience, as I think it is in yours, to warrant congressional attention to the matter. It seems clear that the banking industry or the banking regulators are very hesitant to do anything about this, as Senator Dodd has been demonstrating clearly. At the moment, outside of the Bank of America, which I congratulate enormously in this matter—they have taken a great lead in attempting to offer solutions—but I call your attention to something I haven't heard anybody mention yet. In Mr. Allison's remarks I heard about commercial accounts which were probably restricted to big commercial accounts, but I suggest to you that this is not just an individual consumer experience.

A small businessman is enormously involved and everybody that I've talked to says, "You bet I'm involved." I gave you an example in my testimony of an actual case of a small businessman. I've got further details of that case where the small businessman deposited a Los Angeles' bank check in his Malibu bank—Malibu is about 50 miles north but it's still in Los Angeles County. They didn't tell him anything at the moment of depositing, but they put in the mail that night that his check will be held from the 16th, which was the date of deposit, to the 24th of the month before the funds will be available. Well, not having said anything to him, as I said, he wrote a $20,000 check to pay his supplier in the east. Of course, the check bounced and his supplier called up and said, "What are you trying to do to me," and his reputation is at stake. In addition, he was attempting to get a 2-percent discount by paying on that day and that's why he had put pressure on a customer to pay him that day, and his $400 discount was jeopardized.

I mentioned this to several small businessmen and they all say they suffer similar inconveniences and losses. So it's not just an individual consumer.

I told you a story of some of my students whose father had sent them a check and they had deposited the father's check and written one to pay their telephone bill. The bank held the father's check so their own check bounced. The telephone bill didn't get paid and the telephone company came and removed the phone and then they're responsible for a reconnection charge.

My overriding concern in this is a matter of overkill. You've kept insisting why do they make 99 percent of the customers suffer to take care of this 1 percent possible loss that the statistics show.

Senator Chafee. Well, I noticed in your chart attached to your testimony that there's Shawmut Bank, to just name one, which holds a Government check from 8 to 10 days. I knew we were in tough shape, but I thought our checks had some credibility.

Senator Dodd. That may make more sense than holding a private check.

Father McEwen. Well, the theory that they give for cashier's checks and Government checks is they may be stolen, you know. That's hardly a consolation to a social security or some other kind of recipient of a Government check.

Senator Chafee. Well, in defense of Shawmut, I've got to suppose that a delay like that involves someone completely unknown to them that has not had any banking relations with them previously. I can only assume that.

Father McEwen. That may well be true. What I'm hoping is that publicity like your attention to this matter will force the banks to devise some system. It's irrational that a man able to send his son to an institution that charges $5,000 or $6,000 a year from New

York or Pennsylvania can't have some system with a local Boston bank that they will recognize his checks, but so far they haven't figured out how to do it.

COMPETITIVE SYSTEM

Senator **Chafee**. Do you dismiss the idea of the competitive system?

Father **McEwen**. I do in one sense. At the moment, there isn't enough knowledge among the consumers about their rights and what's reasonable to expect in this matter and as I develop later—maybe I should say something about that now.

I would hope the competitive system could be pushed to do something, but there's no incentive for them to do it. They give up the float—I asked the Federal Reserve to give us that figure in the July meeting and I don't know whether they will or not, but I asked them to develop that precise figure—how much were the banks making on the extra days that they held the funds of depositors.

Senator **Dodd**. Let me interrupt you right there. I should have asked that and I would like to make that request, that the Fed provide this committee with a figure on bank earnings based on the float. I worked up that formula, but I'll be the first to admit that's based on assumptions that may be erroneous.

Mr. **Allison**. The functions involved will be very heroic, but we will make a stab at it. We certainly will.

Senator **Dodd**. Thank you.

Father **McEwen**. Mr. Chairman, I'm going to read you, with your permission, a comment that I made at this Federal Reserve Board meeting of the Consumer Advisory Council in July at which this subject was on the agenda. I had been angered a little bit by hearing testimony about how few complaints there were and how there had been no great problem. At that time I said,

> Besides that, I don't count the number of complaints. This is a favorite trick which I abhor when I hear it used, just to count the number of complaints and decide whether it's a problem or not. I think we can look at the objective nature of this situation and say to deny customers the use of their money for those periods of time without any rational explanation or reason is wrong, and the banking system shouldn't do it. No matter whether 1 customer or 1,000 complained about it, it is the wrong thing to do. That's why I just don't want to count how many people are complaining. You have to have a number of things come together before people complain. They have to know that there is some law, rule or something else that says the seller shouldn't or can't do this to them. They have to know that there is some agency that will receive a complaint and do something about it. And they have to have more than average will and diligence because only 1 in 10 or 20 takes the time to write or develop a complaint when it comes down to it. But this is the system that's wrong though I agree that if immediate transfer takes place float will disappear.

Some of the banking representatives at that meeting asked me if I would agree that the consumer would lose the float. I said, "All right. I have no objections to that." I don't claim we have any right to the float involved in the delayed payment of checks. Mr. Chairman, you were asking whether immediate payment would mean an unsecured loan to the customer. Well, that might be offset—it's true it would—that might be offset by the other end of the transaction when the bank is getting the opposite of that.

At any rate, that's what I said about complaints and I do believe that surveys, for instance, of the whole population, if that's the way it's being done, probably will give a very minute percentage of actual complaints from depositors because I think this is related largely to the metropolitan areas and the bigger banks.

As banking seems to be getting bigger and bigger, the statistics from that study you were reading—I think you quoted several of them—the statistics show that the bigger banks are worse than the smaller banks in their treatment of the customer. There are more bigger banks that put holds on for longer periods than the smaller banks and that I think is related to the personal or impersonal nature of the relationships between the bank personnel and the customers.

Senator **Chafee**. Maybe the Bank of America representative will dispute you on that last statement, but I can see the point you're making.

Father **McEwen**. Well, they are an exception I think, but the statistics in the surveys that Senator Dodd referred to—the statistics clearly show that the bigger banks are treating customers worse than the smaller banks and I have circled them in this excerpt of the statistics of the banks.

Even on the thing that you mentioned, cashier's checks this table is "all banks," and 18 percent of all banks put a 1- to 3-day delay—this is on page 40 of their study—18 percent put a hold on cashier's checks, but in banks with deposits of more than $100 million, 33.3 percent put a hold on cashier's checks.

Senator **Chafee**. Well, Father, I appreciate your testimony and it seems to me you put your finger on an important point and that is that the banks have little incentive to speed up the payment but, indeed, they have great incentive not to due to the float. The longer they hold the money, the better off they are.

Father **McEwen**. That's exactly right.

Senator **Chafee**. And Mrs. Teeters mentioned that in an interview in a New York newspaper. She stated that there was no incentive, and she was quite right, in the system except the incentive, if you will, to provide better services to the customers, but sometimes that's overborne by the profit that can be made through the float.

Father **McEwen**. Mr. Chairman, may I give you the rest of this excerpt which I transcribed?

Senator **Chafee**. Certainly. We would be glad to have it.

Father **McEwen**. From this July 1981 Consumer Advisory Council meeting, this goes into some greater length than I'm able to go into here into this whole subject.

Senator **Chafee**. Fine.

Father **McEwen**. In addition to that, Mr. Chairman, I have a handwritten copy of a complaint of a law student in Boston and his difficulties—numerous difficulties with the delayed availability problem and I'd like to submit that for the record.

Senator **Chafee**. Certainly.

Father **McEwen**. A common thread running through all these problems, just as my friend in California was not told when he deposited the check but got it the next day in the mail, so this boy was not told or told contradictory things time and again by the bank, and it's this message or failure to deliver the information that's really a problem. If they knew their rights, if they knew who to go to to present a case, it might be different.

In addition to that, I will give you a reference and an excerpt for the record from a new book put out by Mr. Donoghue, of Donoghue money fund fame, "William Donoghue's Complete Money Market Guide." Now the banking industry by its failure to address this problem is going to generate an avalanche of consumer action and complaints, particularly if books like this get read. Donahue writes, "So your bank actually can often have the funds the same day your check is deposited or at the very most 2 days later. What then can you do about the delay in access to your money? Complain. That's what." And he goes on to tell them, "Speak up to the teller who will tell you it's the rule. Then work your way up to the manager and then get the rule waived for your account." [P. 203.]

I will submit this for your record also, but my point is that it's too bad that the banking industry has put itself in this position where only an avalanche of complaining customers is going to make them do anything about it.

I would have liked to have seen at least the Fed declare this an unfair banking practice. You may know, Senator—I will give you a reference to this also—the Fed at one time was considering the possibility of designating remote disbursement as an unfair banking and business practice. Remote disbursement, as you know, is the practice of corporations of going to East Oshkosh or somewhere and sending all their checks out from there in the hope they will get 2 or 3 days delay. The Fed did call that or consider calling that an unfair banking and business practice, and that's what I'd like to see them do. I don't think they ever did it. Well, it says here in this February 1979 bulletin the Board gave the following policy guidance: "The Board believes the banking industry has a public responsibility not to design, offer, promote, or otherwise encourage the use of a service expressly intended to delay final settlement and expose the payment recipient to greater than ordinary risk," and so on.

Senator CHAFEE. Well, thank you very much, Father. We appreciate that testimony and, Senator Dodd, do you have any questions?

Senator DODD. No. Father, I thank you for your testimony. I think you have covered some of the questions I would have had for you.

Senator CHAFEE. That last Fed statement or suggested guidance or whatever it is, I wonder if we might have that?

Father McEwen. Yes, I gave that to you.

Senator CHAFEE. Because I would be interested in that because it might pertain to one of the later witnesses. We appreciate you coming down, Father, and for the fine job you have done.

Father McEwen. Thank you very much.

[Additional material received for the record follows:]

EXCERPT FROM CONSUMER ADVISORY COUNCIL, TO THE FEDERAL RESERVE BOARD AT MEETING IN JULY 1981

The more I hear of this subject, the more I get exercised by it. As I listen to all you from the banking industry, it's clear that you're admitting there is no national banking system in this country and that's a disgrace to banking. The fact that your son, if he were in Boston, would have difficulty cashing your personal check Dick, that's ridiculous. And you mentioned, get bank checks and certified checks. If you look at this survey taken in 1978 by the Fed, you'll find that there's practically no distinction between personal and certified checks. They refuse bank checks, cashier's checks and money orders just as much, or almost as bad as they do personal checks. I'm glad to hear Mary admit that it is a problem and I'm distressed to hear the Feds say it's not a problem or that they have doubts about it being a problem. Every one of these documents that I have read I thought had agreed that it is a problem and if the banking industry doesn't think that the failure to have a national banking system available to these consumers in this country is a problem, then I'm disappointed in banking. Let me just refer to the survey. This was not given to the members but I analyzed the contents of it. This was a survey published in 1979 and taken in 1978 and it's a random sample of commercial banks. I facetiously call it, the subject matter, I call it "the D.A.F.", delayed availability funds, or the dead-on-arrival funds, which is more accurate from a consumer point of view. But at any rate, they were identified as a major consumer complaint to be surveyed a way back. This is five years old, this issue was identified by the Fed. The definition incidentally intrigues me.

Banking industry defines the collection period as "the period that it takes for the check to go to its destination and come back as denied." Well, that's a non-collection period instead of a collection period though again, my friends in the banking industry are using queer terminology. Collection period means non-collection period and all sorts of implications flow from that, in my judgement. At any rate, from this survey, and mark you, the survey and the reports make a good distinction between new accounts, new customers and existing accounts, and almost all these data in this survey pertain to existing customers about whom even the, let me get the Bank America Study, says that at the most, a bank should have a fix on a customer in 90 days. And if it hasn't, there's something wrong with the bank. At any rate, I'm sad to say from—I'm glad to hear Dick's comments—because the survey on Page 25 in the data of all banks seems to make out that the bigger banks are worse than the smaller banks, far worse than the smaller banks in the treatment of customers. For instance, the question was asked, "When a bank customer who has an existing personal savings or checking account at the bank deposits a check, is it bank policy or practice to temporarily delay availability?" Of all the banks, 38 percent said, "Yes, that's our policy." Of the big banks over $100 million dollars in deposits, 52 percent said it was their policy to do that. And next question, "Does the teller inform the customer of the fact that it's going to be policy to put a hold?" Only 75 percent of the banks told the people, 25 percent of them never tell them unless they are asked. Again, the discrepancy between big and small banks is here. 25 percent of all banks follow that policy of not telling except when asked, but 38 percent of the big banks have the policy. Flexibility—less than 10 percent admit to frequently altering the policy and there are some strange anomalies in this data that intrigue me no end and make me wonder about Dick's suggestion that if you got a bank check or a certified check, you'd be better off. It seems to me from the data that even same city checks, 28½ percent of cashier's checks in the same city have to wait between one and six days. 46 percent of payroll checks in the same city have to wait one to six days and 63 percent of personal checks have to wait one to six days. Out-of-state checks is outrageous.

Fourteen and one-half percent have to wait thirteen-plus days for an out-of-state check. That's what makes this idea of us having a national banking system appear ridiculous to me if those kinds of waits are true. And in the out-of-state, all kinds of out-of-state checks are treated badly, worse by the bigger banks than by the smaller banks. So much for the survey.

The final Task Force Report from the Fed. had three or four suggestions that seemed to me to miss the point of the problem completely. They just say that policy should be written, it should be defensible and disclose and something should be done for new customers. That seems to me to be the essence of the Task Force Report. I am intrigued by the figures that are given for the actual losses recorded and involved. The return percentge of all checks processed in the last survey that they report to you was 0.6 tenths of one percent of all checks returned for any reasons whatsoever. The actual loss is ridiculously low in money terms. It was five million dollars estimated for the whole banking system. Read the figure in the report, Dick, that's where it came from. Your bank, Dick, seems to have a disproportionately large share of that five million dollars. I worry about you. Now I suggest that when six tenths of one percent is the problem area, why penalize all the other 99½ percent of the check writers and check submitters in the United States? It seems to me to be a ridiculous thing for banking to do and I just can't understand why the figures on complaints may be deceptive because you bankers may be getting a black eye without people realizing that there's something that they should complain about. They just say, "Well, that's just the banker and what can you expect?" I must say that the conclusion of the Task Force Report, Page 10, is the following and is much better than anyone who has spoken here yet has said. The Task Force believes that policies and so forth governing delayed funds availability should encourage banks to identify and protect themselves and their depositors against crime and risk associated with financially irresponsible individuals. Banks should retain the flexibility to provide established financially responsible customers with funds availability should encourage banks to identify and protect themselves and their depositors against crime and risk associated with financially irresponsible individuals. Banks should retain the flexibility to provide established financially responsible customers with funds availability on a schedule at least equal to the receipt of provisional credit by the bank without extending similar funds availability in situations that involve crime. Now the provisional credit is the immediate one day or at most, two days. So at least the Task Force has come out by saying, "We recommend that the maximum delay should be for the period of provisional credit." I go further and say I don't think there's any justification for any delay given the miniscule proportions and percentages involved. I realize that there are U.C.C. problems in the return process and that the Fed. has taken an attitude—the history of the Fed. involvement is curious—it was in the 1979 Annual Report to Congress, apparently it was on the agenda for the C.A.C—this group's discussion in February of 1979. In September of 1979, Governor Caldwell gave a speech to the bankers in which he told them it was a serious problem that they better do something about, and in October of 1980 Chairman Volcker gave a speech in which he said it was also a problem that should be solved by self-action on the part of bankers.

In the light of this history of five years of sort of foot-dragging by the Fed. and needling of the banking industry to do something by itself, I think it's ridiculous that we sit here and talk about disclosure and education and I don't want to educate the customer to think that he has no right to his money. I'd rather educate the customer to think that the banking industry is smart enough to figure out ways of taking care of giving him his funds right now without any of this ridiculous delay.

Mr. Chairman, I want to congratulate the authors of that Bank of America study because they have identified the history of this problem and they have identified their own banks' policy, I think, in an exemplary fashion. I just suggest that this is a disgrace on the banking industry of the United States, these figures. And if you in the banking industry can't do better than this, then I'm disappointed.

Peter, the float—I don't claim—I don't know where you got the idea that we claim that as a right. I don't claim float as any right for a customer. I do claim immediate availability of deposits as a right to every customer and I vehemently object to the Fed., to Margaret, and anyone who just counts heads of complaining customers to decide whether it's a problem or not. 99 percent of the customers in this banking system are being denied the use of their money for anywhere from four to thirteen days. Then I would ask the Fed. to develop a monetary figure on how much interest the consuming public is losing by the inability to have access to that amount of money for those number of days, and I think it would be a considerable amount of money. Becides which, I don't count the number of complaints you know, this is a favorite trick which I abhor when I hear it used, just to count the number of complaints and decide whether it's a problem or not. I think we can look at the objective nature of this situation and say to deny customers of the use of their money for those periods of times without any rational explanation or any reasons or justification is wrong, and the banking system shouldn't do it. No matter whether one customer or a thousand complained about it, it's the wrong thing to do. That's why I just don't want to count how many people are complaining. You have to have a number of things come together before people complain. They have to know that there is some law or rule or something else that says that the seller can't do this to them. They have to know that there is some agency that will receive a complaint and do something about it and they have to have more than average will and diligence because only about one out of ten complains, when it comes down to it. But this is a system that's wrong. I agree with you that as the immediate transfer takes place, float will disappear and that's a trade-off that I'll be willing to give.

RE ONE CONSUMER'S DIFFICULTIES AT SHAWMUT

This September I opened a checking account and savings account at Shawmut Bank at the advice of friends. After persistent troubles, coupled with an overall lack of cooperation by the bank's officers, I closed my accounts taking my business elsewhere.

As a new Bostonian at this time, part of my resettlement consisted of taking funds from other accounts (located in New Jersey) using cashier checks and depositing them in the Shawmut accounts. These transfers were necessary to cover not only everyday living expenses, e.g., book costs for law school and rent and security for a new apt. My difficulties at Shawmut began at this point.

One check I deposited was in the amount of $300. I assumed it would take only four-to-five days to clear, since when I opened my account at Shawmut, I opened it with a cashier's check for a similar amount. I used money from that within four days approximately. Thus I assumed the same amount of time would be involved with respect to the second check.

It was not until approximately two weeks later that this second cashier's check cleared, so I learned to my dismay I had withdrawn money ($25.00) from my checking account. This reinforced my belief that the check had cleared. Several days later I went to withdraw some more money, but this time I was told there was a hold on my account. The teller directed me to a bank officer.

(This particular officer (Ms. June Cooke) was throughout my ordeal a sympathetic individual who sought to mitigate my difficulties, unlike other officers I dealt with.)

I asked her how I could have withdrawn money earlier. She didn't know. Moreover, the teller had told me my account balance which contradicted my calculation. It also contradicted Ms. Cooke's calculation. She called a main office to find out whether the check had cleared. Not only did she learn that it did not, she also found out that 3 checks I made out (on the premise that the cashier's check cleared) were sent back! One of the check's was for law books. To cap it off, a fourth check I made out (before the other 3) cleared!

Ms. Cooke then directed me to a higher officer who proved belligerent and incooperative. He contended that a cashier's check took as long as a personal check to clear. I asked him (1) what was the purpose then of getting a bank check and (2) why my first bank check cleared in a much shorter amount of time. Nor did he respond to me when I pointed out that even Ms. Cooke conceded that this check was taking an inordinate amount of time.

He contended that the teller several days back made a mistake in cashing my check. But then so I contended, did the place of processing when one of my checks cleared. Moreover, by the teller cashing that check, she was telling me my account was fine. Also, I was never sent notice that 3 checks were returned.

I expressed concern about this since I had a cashier check for $1,100 to deposit. This was to go in part to cover rent and security. I wanted no problems with this.

Alas, there was.

On different occasions, tellers and bank officers obtained different balance results on the machines. One woman officer received a balance of zero! Meanwhile more checks bounced. Finally I closed my accounts.

Post-script: I now bank at First National where my cashier checks clear in a matter of days. Furthermore, their balances square with mine.

Nor should it be left unmentioned that I requested of the male officer that he write to those who received my checks back, telling them that the problems were bank-related and not because of personal culpability on my part. He refused. He asked how could I explain how it was the bank's fault. I responded that I wasn't acquainted with banking, that I relied upon him to find out. I pointed out that the problem evidently incompassed more than the time it took for any cashier checks to clear, since there were simple problems it computing my balance. It could have been a problem with the way my account was being computerized.

Mistakes do happen. However, when they are persistent, and the consumer is made culpable, there is no excuse.

JAMES BRINNING.

[From Donoghue's Complete Money Market Guide]

CHECK THIS OUT

At the opposite end of the money-moving spectrum from the instant transfer is check cashing, particularly if the check is an out-of-town one. Many banks will place a "hold" on a check for ten days, supposedly to make sure it clears. That means the bank has the free use of your money for a week and a half while you're left eating baloney.

For that's exactly what it is. A check does not take ten days to clear, nor are banks required to wait for that period of time before giving you access to your money, as so many of them claim. The ten-day rule, and in some banks the period is as long as twenty-one days, is strictly an internal regulation—one to which, with good banking relations, there's no need for you to be subjected.

The actual clearing process for a check, in almost every case, involves its passing through the Federal Reserve. And back in the old days, when checks made their way leisurely across the country stuffed in the mail sacks of transcontinental trains, the ten-day rule had some basis in reality. Today, however, the clearance is done by computer, with checks flying back and forth overnight in their very own special jets. As Ellen Stockdale, at the office of the Comptroller of the Currency in Washington, points out: "It's not hunks of money being physically transferred from one bank to another. It's all done on computers. The minute that the Fed gets a little electronic impulse for your particular check, your bank is credited."

AVOIDING UNNECESSARY "HOLDS" ON YOUR CASH

So your bank actually can often have the funds the same day your check is deposited or at the very most two days later. What, then, can you do about the delay in access to your money? Complain, that's what.

Speak to the teller, who will tell you it's the rule. Then work your way up, right up to the manager if necessary, until you get the rule waived for your account. If you are a good customer, it can be done, believe me. I've done it, and now I can use the money behind any checks deposited the same day. And don't think it's just because I happen to be involved in the financial world. According to a Federal Reserve study, 97 percent of the banks surveyed said they could alter their check clearance policy to accommodate customers. If your bank is one of the other 3 percent, find a new bank.

Money does come in two varieties, instant and delayed. Now, by delayed money I don't mean credit, which, of course, is also a form of spendable money. No, delayed money is funds that are actually deposited to an account but for the moment cannot be used, the kinds of funds, for instance, that your bank has when you deposit a check drawn on a different bank. Your bank does have to clear that check through the Fed. Once it's cleared, however, it becomes Fed funds, or Federal Reserve funds. And that's real money, available to the bank and to you.

This answers the second argument the bank will give you when you try to persuade them to give you instant use of any checks deposited. The argument that your checks must clear the Fed is valid, but it is valid for, at the most, only two days. And, as I've said, if you're a good customer, the bank should be willing to waive even this waiting time. After all, even if it takes two days for your deposited check to become real, genuine money (Fed funds), any check you write against that deposit will take the same amount of time to get back to the bank plus the time "your check is in the mail." At no time will the bank be out of funds. All it will be out is the free interest it's been collecting for years on your account. Now you know what the bankers mean when they say they're "enjoying the relationship."

Maybe the bank won't let you spend the $12,500 check you receive for selling your boat because it's worried about that particular check's collectibility. In other words, you're not in the habit of making deposits of that size, and it might bounce. In this particular case, the two-day clearance for funds doesn't really apply. Oh, the bank does get $12,500 worth of Fed Funds within two days, but the check could still bounce when it is sent on to the bank of origin, in which case the Fed would take back its funds from your bank. There is a legitimate reason, then, for a bank to hold back funds represented by a large check of unknown collectibility.

So let's not be petty about it. It's not worth switching banks for one check. Besides, in the span of time it would take you to find a good alternative bank and switched accounts, your original bank would probably have collected on that once-in-a-blue-moon check. Does that mean you should just deposit it and accept an interestless ten days?

Certainly not. Deposit the check to your savings account instead, and you will draw interest from the day of deposit. The instant-and-delayed money distinction does not usually apply to the interest-paying facet of savings accounts. You merely will not be allowed to withdraw on the capital amount until the check has cleared.

Then again, you have another alternative. You can simply endorse the check over to your money fund account. In that case you've invested almost as quickly and at a considerably higher yield—assuming the stop-and-start post office is making deliveries that week and you don't use the postage-paid return envelope supplied by the money fund. But call the fund first and inquire about their policy on "third-party" checks.

LICKING THE STAMP DELAY

Saving a postage stamp will cost you a day's worth of dividends, or even more from a money fund. The fact is that the post office doesn't accord first-class service to postage-paid return mail. It spends an extra day accumulating the envelopes, counting the postage due, and charging the money fund's account. Of course, postage-paid mail isn't supposed to take longer. But the facts speak for themselves, as people who have availed themselves of this service can attest.

If New York City is the United States financial center, it's also the snafu center of the post office. Postal service is so fouled up that some Wall Street-based funds have resorted to using Newark, New Jersey, post office boxes, just to accelerate delivery. If you make numerous small deposits to your money funds by mail, chosing one located in California makes sense even if you live in, say, Boston, solely on the consideration of speeding up your deposits.

Our Holliston—outside Boston—office receives next-day mail service from California, whereas it may take five days or more to receive first-class mail from New York. Even ten or twelve days is not unusual. Special delivery, of course, adds additional time to your money's transit period.

WHEN TO WIRE

If you have more than $10,000 to transfer, it usually pays to move your money by wire. Please don't confuse wiring with Western Union, which can be even slower than the U.S. postal system, particularly on international transactions. To move large sums of money efficiently, the Federal Reserve wire system is the only way to fly. This wire system ties together all the Federal Reserve member banks. It's a private communication system for transferring funds. And since it's the big boy's money that's involved, the system is swift and efficient. Money is deducted from one account and deposited to another simultaneously. Not a moments' worth of interest is lost.

Senator CHAFEE. All right. The next panel, Mr. Pickell, senior vice president, Old Stone Bank, Providence, R.I.; Mr. Heron, senior vice president, Citibank; and Jacquie Del Bucchia, manager of customer relations, Bank of America. Will you come up to the table and we'll take your testimony.

We welcome you here and I would ask that—we have your testimony. Of course, we will put these in the record. We want to save some time for the questions so we would ask that you summarize your statements and that would then leave a little more time for questioning. So why don't we take them just as we listed them on the docket here. Mr. Pickell, why don't you lead off.

STATEMENT OF BARRY PICKELL, SENIOR VICE PRESIDENT, OLD STONE BANK, PROVIDENCE, R.I.

Mr. PICKELL. Thank you, Mr. Chairman.

It is my pleasure to appear before your committee to review Old Stone's policies and procedures for funds availability on consumer banking deposits.

[Complete statement follows:]

TESTIMONY

OF

BARRY PICKELL, SENIOR VICE PRESIDENT

OLD STONE BANK

Mr. Chairman, my name is Barry Pickell and I am a senior vice president of Old Stone Bank which is headquartered in Providence, Rhode Island. It is my pleasure to appear before your committee to review Old Stone's policies and procedures for funds availability on consumer banking deposits.

As background, it may be helpful to know that Old Stone Bank is the second largest financial institution in Rhode Island. Its assets total $1.7 billion. Old Stone has a large consumer banking business, consisting of approximately 280,000 consumer checking and savings accounts which it services through 35 statewide offices.

Old Stone Bank uses three sources for clearing checks drawn on other banks that are deposited to customer accounts or cashed at our teller windows. These sources include the Providence Clearing House, which clears checks for the major Rhode Island commercial banks, and two correspondent banks, one of which is located in Boston and the other in Hartford. The Boston correspondent clears checks drawn on New England banks and the Hartford bank clears all other domestic checks. Old Stone does not send any checks directly to the Federal Reserve for check clearing.

Checks exchanged through the Providence Clearing House with other local banks account for over 50% of Old Stone's outgoing items. We receive credit for these checks on the day they are presented for payment. For example, clearing house items which are deposited at our bank during business hours on Monday are sorted into paying bank order on Monday evening at our Operations Center. These checks are exchanged at the Clearing House on Tuesday morning at which time we receive immediate credit from the other clearing house members. Similarly, we provide immediate credit to other clearing house banks for the checks drawn on Old Stone which they present to us.

In the case of check clearing through our Boston and Hartford correspondents, the period of time before Old Stone's account is credited is slightly slower. Again, using Monday's transactions as an example, all out-of-area items are sorted by our Operations Center personnel in accordance with which correspondent bank will handle the check clearing to the paying banks. Between 5:30 and 8:30 p.m. Monday night, the batches of out-of-area checks to be cleared are picked up by couriers and delivered by land and air to our correspondents in Boston and Hartford. Our Boston correspondent credits Old Stone's account on Tuesday for about 95% of the value of all Monday's work received with the balance being credited on Wednesday. The Hartford correspondent provides 85% credit on Tuesday for work received Monday night, and the remaining 15% is credited on Wednesday.

The foregoing describes, in general terms, how our check clearing system works and when Old Stone Bank receives credit for checks cleared. Let me turn now to when we credit our customers' checking, NOW, or savings accounts for checks deposited to them. Again assuming that the customer makes a deposit on Monday, his checking, NOW, or savings account is updated at our Operations Center on Monday evening and he will have use of the funds on Tuesday. In other words, cash withdrawals can be made against the customer's ledger balance on Tuesday at our branch offices. A customer, however, cannot obtain a certified check from funds deposited by check on Monday until Wednesday.

Old Stone also receives debits and credits to customer accounts by magnetic tape from the New England Automated Clearing House. The majority of these items represent periodic government payroll and social security payments. Customer accounts are credited or charged in accordance with instructions received on the tape. The Bank receives an equivalent credit or charge to its account at a Boston correspondent from the originating bank on the effective entry date specified on the tape.

We believe Old Stone's present policies for crediting customer accounts are quite generous. They may account, in part, for our favorable experience in checks returned for insufficient funds which averages less than 3/4 of one percent. Nevertheless, we do have safeguards built into our various deposit accounting systems which help to protect the bank from abuse and fraudulent activity.

Old Stone has automated its teller operation and this system now functions in an on-line mode. The system requires that tellers access a computerized data file through terminals located at their work stations whenever checks are cashed against customer accounts or withdrawals made from NOW accounts and savings accounts. Holds are automatically placed against ledger balance funds so that accounts cannot be knowingly overdrawn.

Our on-line system also will indicate to the teller the date that an account has been opened and the date and amount of last deposit. Tellers, therefore, are alerted to possible frauds through attempted cash withdrawals from accounts which had just been opened and funded with a deposit made by check drawn on another bank. Tellers, subject to branch managers' approval, may refuse withdrawals from such accounts until the check deposited has cleared.

Additionally, Old Stone's Operations Center supervisor constantly monitor our check processing system for kites and other abuses. The success of their efforts is best evidenced by the low level of losses experienced by the Bank.

This concludes my remarks. I shall be pleased to answer any questions you may have.

Senator **Chafee**. Well, thank you, Mr. Pickell. I think what we will do is take all three of the witnesses' statements and then we'll proceed with the questions.

Mr. Heron, your statement is of some length and in order to again—why don't you take 5 minutes any way you wish. You can read it. You can summarize it. But the time limit is 5 minutes.

STATEMENT OF WILLIAM HERON, JR., SENIOR VICE PRESIDENT, CITIBANK

Mr. **Heron**. Mr. Chairman, I have a truncated version that I will contain within the 5-minute limit.

Mr. Chairman, Senator Dodd, my name is William Heron and I'm a senior vice president of Citibank, N.A. in the New York banking division, which offers individual and small business banking through more than 260 branches in the New York metropolitan area.

I am pleased to have this opportunity to discuss the subject of check clearing and availability of funds. Comments in the press indicate the subject is widely misunderstood and often oversimplified. Banks are mistakenly thought to derive great profits at the expense of customer convenience. However, we have long been aware of the importance of prompt check cashing, availability to our customers. In fact, we consider it to be an important element in the rigorous fight for the consumer dollar in New York and have been working to eventually eliminate delay altogether.

We know that when it comes to choosing a bank, consumers weigh many considerations. A funds availability policy is just one of these. The right combination of services will bring in customers and keep them satisfied. The wrong combination will drive them away. That is the basis of competition.

Our present policy has evolved steadily since 1975. We hope that it will be another good reason for consumers to choose Citibank over other institutions.

MAJOR FEATURES

The policy now has four major features.

First, we make available at least $25 from deposited checks.

Second, we start paying interest on deposits to NOW accounts and other interest bearing accounts on the day of deposit. This is before we have credit for these funds from the Federal Reserve, although these funds would not normally be available to the customer until the check has cleared.

Paying interest on these newly deposited funds costs Citibank money, but we do so because it makes our services more attractive to the public.

The third component of our policy is that we do impose a selective schedule of delays on the clearing of checks, ranging from zero to 15 days, depending on the location of the issuing bank in order to give ourselves reasonable assurance that checks deposited at Citibank are good. It is our job to protect both the stockholders and customers who eventually absorb the cost of fraud.

I might add that 90 percent of these checks are available in 3 days or less. So at issue for us today are at most 10 checks out of every 100 drawn on out-of-town banks. Half of all deposited checks are for amounts small enough to qualify for immediate availability. When you consider that most of our customers maintain balances high enough to cover their immediate needs, the problem becomes very small indeed.

To solve this problem, we began work more than 2 years ago on the fourth major feature of our funds availability policy. We brought our expertise in electronic banking to bear on the funds availability problem.

Our success with electronic banking is indisputable in our marketplace. Customers endorsed our services with over 70 million transactions at our Citicard Banking Centers last year. We now provide, or will shortly, a number of services just as convenient, which make deposited funds available immediately.

Individual customers can sign up for our overdraft accounts, which we call checking plus. Those who qualify are granted a line of credit.

But this is not just an ordinary overdraft privilege. The checking plus customer can get cash immediately for new deposits because he is already adjudged a good credit risk. There's no charge or interest for this service.

We have a plan on the verge of introduction so new that we don't even have a name for it. This one is an unprecedented expansion of consumer electronic banking which will allow customers instant access to new deposits 24 hours a day, 7 days a week.

Here's how it works. If you have a Citicard day-to-day savings account, certain time deposits, or even a high-yielding money market certificate of deposit, you can deposit a check in your checking account through an automatic teller machine and immediately draw cash, write checks, or make payments up to the combined balance in all of your accounts.

These four elements, then, comprise our funds availability policy.

Some of our customers have fond memories of an age in which a handshake and a good record were all that were necessary for cashing checks, and they wonder why things have changed. For the past 2 years, we have been trying to create something we'd like to think of as an electronic handshake.

For those customers who don't take advantage of our services, however, there remains the problem of delay. The fact is, a substantial number of checks are returned to us. In a typical day, this amounts to approximately 4,000 checks. If we permit customers to draw money against these bad checks, it is Citibank's loss which, as I mentioned earlier, is borne by our shareholders and customers.

There are many reasons why newly deposited checks bounce. A concern for our organiation is fraud. Five years ago our losses were large and they were growing rapidly. We have reduced losses significantly, but they still come to about $1 million a year.

To understand why Citibank delays availability of funds, it is necessary to picture the system through which checks are presented for payment. But, rather than describe the check-clearing process, some of which has been covered by other witnesses, I will skip over some of my testimony.

We have a schedule updated periodically which is geared to actual return times for banks in various Federal Reserve districts, and we stick to it, no matter what the weather is like. We have a set delay schedule and we constantly monitor and adjust this schedule accordingly.

As far as the bank of deposit is concerned, it must allow for the check itself to be returned. In the meantime, the deposit bank is left wondering whether a normal transaction has taken place or a fraud perpetrated.

Some bank customers, including criminals, take advantage of these delays in several ways, all of which fall under the designation of "kiting."

The best explanation of how a criminal kites checks was given in a book called The Check Book, published on the west coast in the midseventies. "The Check Book" was written by one "Hot Ralph," a self-proclaimed "professional crook."

Ralph defines check kiting as "the building up of large apparent balances in one or more bank accounts, based on uncollected checks drawn against similar accounts, based on uncollected checks drawn against similar accounts in distant banks, for the purpose of using money without interest, or siphoning funds from the inflated accounts."

There are many Hot Ralphs out there and they are making off with lots of money that belong to other people. They are resourceful. Every time a new procedure is developed to prevent fraud, they find out how it works.

Still, to say that fraud exists and to describe its magnitude does not address the plight of the honest customer who is disturbed because his checks are bouncing.

Certainly the customer is entitled to convenient service and access to his fund. This is why we are offering services designed to meet these customer needs. There is a popular conception that banks hold uncollected funds longer than necessary in order to earn extra income.

At Citibank, extra income from holding funds is an insignificant factor because we are paying interest from day of deposit. Most of our customers hold sustantial balances, which can be used while their deposited checks are clearing. Those old balances dwarf new deposits.

To reiterate, our funds-availability policy is based on our customers' convenience, reconciled with a reasonable need to protect ourselves against fraud.

The need to please our customers is drawing us toward a system in which the inconvenience of delayed funds is eliminated through electronics.

Senator CHAFEE. Mr. Heron, I'm afraid your 5 minutes are up.

Mr. HERON. Thank you, Mr. Chairman.

Senator CHAFEE. Is there any major point in here in addition you wish to make?

Mr. HERON. I would like to make one comment and we suggest and respectfully submit that the issue is more than delayed funds availability; it is competition and, in fact, there are organizations who can emulate the means of traditional consumer banking while paying market rates of interest which depository institutions such as ours are not permitted to do. We do look forward to the hearings of the Depository Institutions Deregulation Committee meeting of

March 22, and do hopefully anticipate that more progress will be made in terms of deregulation of interest rates currently under Regulation Q.

[Complete statement follows:]

STATEMENT OF
William J. Heron, Jr.
Senior Vice President
Citibank

My name is William Heron. I am a senior vice president of Citibank, N.A. in the New York Banking Division, which offers individual and small business banking through more than two hundred and sixty branches in the New York metropolitan area.

I am pleased to have this opportunity to discuss the subject of check clearing and availability of funds. We have long been aware of the importance of prompt cash availability to our customers.

In fact, we consider it to be an important element in the rigorous fight for the consumer dollar in New York.

We know that when it comes to choosing a bank, consumers weigh many considerations. A funds availability policy is just one of these, along with location of branches, interest rates, fees, and so on. The right combination of services will bring in customers and keep them satisfied. The wrong combination will drive them away. That is the basis of competition.

Our present funds availability policy has evolved steadily since 1975. We hope that it will be another good reason for consumers to choose Citibank over other institutions.

The policy now has four major features.

First, we make available at least twenty-five dollars from deposited checks.

Second, we start paying interest on deposits to NOW accounts and other interest bearing accounts on the day of deposit. This is before we have credit for these funds from the Federal Reserve, although these funds would not normally be available to the customer until the check has cleared.

Paying interest on these newly deposited funds costs Citibank money, but we do so because it makes our services more attractive to the public.

The third component of our policy is that we do impose a schedule of delays on the clearing of checks, ranging from zero to fifteen days, depending on the location of the issuing bank. We do this in order to give ourselves reasonable assurance that checks deposited at Citibank are good. In our banking system with its mix of paper and electronics, there are ample opportunities for fraud. If fraudulent checks are deposited or cashed at Citibank, the loss is absorbed by our stockholders, and ultimately by our customers. It is our job to protect both these groups, and one way to do so is to impose a delay before newly deposited checks can be drawn on.

I might add that ninety percent of these checks are available in three days or less. So at issue for us today are at most, ten checks out of every hundred drawn on out-of-town banks. Half of all deposited checks are for amounts small enough to qualify for immediate availability. When you consider that most of our customers maintain balances high enough to cover their immediate needs, the problem becomes very small indeed.

However, when customers do not maintain balances adequate to cover the checks they write, we are faced with a problem. We must serve our good customers and minimize losses.

To solve this problem, we began work more than two years ago on the fourth major feature of our funds availability policy. We brought our expertise in electronic banking to bear on the availability problem.

Our success with electronic banking is indisputable. Customers endorsed our services with over 70 million transactions at our Citicard Banking Centers last year. Withdrawals alone came to over forty-five dollars every second of the day, year round. We now provide, or will shortly, a number of services just as convenient, which make deposited funds available immediately.

We offer direct deposit of payroll, similar to direct Social Security deposit, which eliminates delays. A magnetic tape of a corporate payroll credits employee accounts automatically, at the bank of the employee's choice. There is a secondary benefit to employers, who not only save certain operating costs but also any time their employees might lose while standing in bank lines to cash their checks. For us, it eliminates the risk of forgery and theft, which are present when cashing payroll checks.

Individual customers can sign up for Checking Plus. Those who qualify are granted a line of credit.

But this is not just an ordinary overdraft privilege. The Checking Plus customer can get cash immediately for new deposits, as surely as he could with a bank officer's signature, because he is already adjudged a good credit risk.

Say you had a two thousand dollar credit line, and you deposited a five hundred dollar check. You could then draw out the entire amount in cash right away at a Citicard banking center. This would be a great help in cashing a weekly paycheck. There is no charge for this service. Nor would any interest be charged for it, unless the newly deposited check happened to bounce. Then it would be subtracted from your credit balance.

We have a plan on the verge of introduction so new that we don't even have a name for it. This one is an unprecedented expansion of consumer electronic banking, which will allow customers instant access to new deposits twenty-four hours a day, seven days a week.

Here's how it works. If you had a Citicard Day-to-Day savings account, certain time deposits, or even high-yielding money market certificates of deposit, you could deposit a check in your checking account through an automatic teller machine and immediately draw cash, write checks, or make payments. You wouldn't even have to wait for the check to be processed. Interest would be paid from day of deposit, even on weekends. If the deposited check turns out to be no good, no interest would be charged, but the customer will be asked to make up for any cash withdrawn or checks written against it.

These four elements, then, comprise our funds availability policy.

Some of our customers have fond memories of an age in which a handshake and a good record were all that were necessary for cashing checks, and they wonder why things have changed.

For the past two years, we have been trying to create an electronic handshake.

In head to head competition, we feel, our service looks pretty good. If some other bank tops us, so much the better for the customer. Then we will try to do better still.

For those customers who don't take advantage of our services, however, there remains the problem of delay. If all we are doing is trying to replicate the traditional banker-customer relationship, why does a delay policy exist?

It would appear that a delay policy could drive away some customers. Again, that is a business decision we have had to make.

The fact is, however, that a substantial number of checks are returned to us. In a typical day, this amounts to about 4,000 checks. These are not confined to new accounts, but often involve customers of long-standing. If we permit customers to draw money against these bad checks, it is Citibank's loss, which, as I mentioned earlier, is borne by our shareholders and customers.

There are many reasons why newly deposited checks bounce. There are stopped payments, insufficient funds, closed accounts, lack of endorsement, and so on.

A major concern for Citibank, however, is fraud. Five years ago, our losses were very large and they were growing rapidly. We have since reduced losses significantly, but they still come to almost a million dollars a year.

To understand why Citibank delays availability of funds, it is necessary to picture the system through which they are presented for payment.

Checks are cleared only after changing hands several times, the number usually increasing with the distance they must travel. Most people think that it is all done electronically, but this just isn't so.

For example, a check drawn on a New York bank and deposited at Citibank is credited to the Citibank customer and begins earning interest right away. At this point, it is classified as uncollected funds.

From there the check goes to the New York Clearing House, and then to the bank on which it was drawn. If this bank decides not to pay, the check retraces its path back to the bank of deposit. It takes three computer postings, one for each business day, before the amount is cleared for withdrawal.

Excluding holidays, this means that a check deposited on a Monday will be available to pay checks presented on the following Thursday night and for check cashing the morning after that. Three business days can almost become a full week, as far as the customer is concerned, if a weekend intervenes.

Checks from more remote locations take longer to clear because there are more clearing houses, more banks, more intermediaries of all kinds, not to mention the possibility of human error, computer failure, and acts of God.

When a Citibank customer deposits a check from a small California bank, for example, it may go from Citibank to the New York Fed, the San Francisco Fed, a large California bank, and then the issuing bank. Or, depending on the amount, it may be sent by courier to a correspondent bank in Chicago, a major clearing center, and then to another correspondent in California. Each step will take between half a day and a day and a half.

Transportation is seasonal. Even a minor airplane delay can add a day or more. Imagine what this winter's blizzards in Chicago meant to check clearing.

Almost ninety-nine percent of checks deposited at Citibank are not returned. If a check is not paid, however, it must return to Citibank following via the same path it took to get to the bank on which it was drawn. The time from deposit to redebiting for a returned check is three business days for a New York City check, as I said, but it takes about six for a suburban New York check, and about nine for a California check. Add a couple of weekends and you're talking about more than two weeks.

Still, we have a schedule we follow, which is geared to actual return times for banks in the various Federal Reserve districts, and we stick to it, no matter what the weather is like. The schedule is periodically updated according to changes in actual return times.

As far as the bank of deposit is concerned, it must allow for the check itself to be returned. We hope it will never reappear. No news is good news. It is not a simple task, however, to distinguish between no news that is good news and no news that means a bad check is in the process of being returned but has not yet arrived. In the meantime, the deposit bank is left wondering whether a normal transaction has taken place, or a fraud perpetrated.

Some bank customers take advantage of these delays in several ways, all of which fall under the designation "kiting."

The depositor may deliberately draw against uncollected or insufficient funds, fully intending to cover the amounts drawn before the checks are presented for payment.

Or the depositor might draw against uncollected funds to purchase goods or pay for services.

The form of kiting of most concern to us, however, involves cashing checks deliberately drawn on an account whose balances have been inflated by the deposit of bad checks.

The best explanation of how a criminal kites checks was given in a book called The Check Book.

The Check Book was written by one "Hot Ralph" a self-proclaimed "professional crook," who grew up "in the streets and in the prisons" who claims to have "no so-called morals."

Ralph defines check kiting as "the building up of large apparent balances in one or more bank accounts, based on uncollected checks drawn against similar accounts in distant banks, for the purpose of using money without interest, or siphoning funds from the inflated accounts." Ralph continues, "Did you understand that? It took me a week or so to really catch on, so don't feel too bad."

That is the stated purpose of this book. I won't go any further, as I see no reason to make this field of knowledge part of the public record. Suffice it to say, however, that the aspiring felon is taken from the rudiments of check kiting up through a blueprint for million dollar bank fraud.

There are many Hot Ralphs out there, and they are making off with lots of money that belongs to other people. They are resourceful. Every time a new procedure is developed to prevent fraud, they find out how it works. When we change the threshold for automatic setting of uncollected funds in order to foil potential frauds, they find out about the new threshold, and write their checks accordingly.

Some of them are no longer banking at Citibank, although remarkably few of them are prosecuted or jailed. But they are still out there, kiting checks with other, less rigorously controlled banks.

Still, to say that fraud exists and to describe its magnitude does not address the plight of the honest customer who is disturbed because his checks are bouncing.

Certainly, the customer is entitled to convenient service and access to his funds. This is why we are offering services designed to meet these customer needs.

There is a popular conception that banks hold uncollected funds longer than necessary in order to earn extra income.

At Citibank, extra income from holding funds is an insignificant factor because we are paying interest from day of deposit. Most of our customers hold substantial balances, which can be used while their deposited checks are clearing. Those old balances dwarf new deposits.

To reiterate, our funds availability policy is based on our customers' convenience, reconciled with our reasonable need to protect ourselves against fraud.

And as you have seen, we are making it easier for our customers to gain immediate access to new funds.

The need to please our customers is drawing us towards a system in which the inconvenience of delayed funds is eliminated through electronics.

We hope that consumers, faced with a choice of accounts at a wide array of institutions, not just banks, will choose Citibank. We are out to win new customers, but we are also out to retain them by building relationships over time with the best financial products and service available. That's our business.

If consumers choose other institutions, that's their business.

That's what competition is all about.

However, I am sorry to say that the banking industry is not very competitive, and it is the bank customer who suffers.

For example, if a customer wants to combine market interest with liquidity, banks are limited by law in what they can do for him. To fill this niche in the market, money market mutual funds sprang up, and they have attracted $185 billion in just a few years, money that might have gone to depository institutions if they had been allowed to compete.

Competition being what it is, the securities industry, through money market funds and other forms of cash management, is drawing closer and closer to the convenience of traditional consumer banking.

For those who champion the cause of the consumer, I would say that the real issue before Congress is competition.

We believe that removal of legal and regulatory constraints would enable all financial service companies to compete on the basis of service and price.

In a truly competitive market, consumers would choose products that satisfied their financial needs.

There is another large issue involved. For years, business people and government officials have been decrying the historically low rate of savings in this country. It is widely held that in order to put this nation back on the track to economic growth, personal savings must increase. Certain measures have already been taken, such as allowing all taxpayers to open Individual Retirement Accounts.

What about money that people plan to use before retirement, however? A comprehensive savings strategy should incorporate that, too.

The Depository Institutions Deregulation Committee will be meeting in twelve days to consider a variety of new products and to start the process of interest rate deregulation. We urge Congress to encourage members of DIDC to carry out its mandate to give consumers, particularly small savers, a fair return on their savings by deregulating interest rates, and provide them with new deposit products as an incentive to save. We also urge Congress to expedite changes of obsolete laws and regulations, which only serve to prohibit depository institutions from offering consumers the best possible financial products and services nationwide.

Thank you. I would be happy to answer any questions you might have.

Senator **Chafee**. Well, we appreciate your getting in a lick for that subject. That's not the purpose of this hearing right now. We are glad to have your position known however.

All right. Mrs. Del Bucchia.

STATEMENT OF JACQUIE DEL BUCCHIA, MANAGER OF CUSTOMER RELATIONS, BANK OF AMERICA

Ms. **Del Bucchia**. Mr. Chairman, Senator Dodd, my name is Jacquie Del Bucchia and I will make my discussion brief.

Senator **Chafee**. Five minutes.

Ms. **Del Bucchia**. All right.

[Complete statement follows:]

March 10, 1982

TESTIMONY OF JACQUIE DEL BUCCHIA BEFORE THE SUBCOMMITTEE ON CONSUMER AFFAIRS OF THE SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS.

Mr. Chairman and Members of the Committee:

My name is Jacquie Del Bucchia. I have been the Manager of the Customer Relations Department of Bank of America for the past two years. Prior to my current position, I had over ten years experience in a variety of positions with the Bank, including teller, loan officer, collections, and new accounts.

I am pleased to be here today to discuss the issue of delayed availability of funds for deposited checks and to describe Bank of America's policies in placing holds on uncollected funds and what we are doing to minimize the delay period.

To understand the issues involved, one must first understand the reasons why holds are sometimes placed for uncollected funds. A bank will place a hold on deposited checks essentially for one of two reasons, either to protect itself from the risk that the deposited check will be returned unpaid by the paying bank, or to avoid the cost of float incurred when its customer withdraws the funds before the bank has received payment on the deposited check from the paying bank. In the latter instance the delay should be relatively short, normally from one to three business days depending on the distance to the paying bank and the number of institutions involved in the clearing process. When protection is the reason, however, the time can be much longer, in some cases over twenty business days. While the check clearing process has made great strides in recent years through electronic and automated procedures, the processing of return items remains a highly manual and labor intensive task. Furthermore, under the Uniform Commercial Code a collecting or paying bank may drop a return item in the mail as late as midnight of the day following receipt of the item. Since return items normally retrace the check clearing path rather than being returned directly to the depository bank, the postal and handling delays can be substantial when several collecting banks are involved. Delay in the physical return of items has become one of the biggest problems contributing to delayed access to customers' funds.

At Bank of America we place holds on certain deposited checks for the purpose of protecting ourselves from the risk of loss on returned items. This risk is significant. A recent survey of our checking operations shows that we receive on an average daily basis approximately $22 million in returned items. Some days that figure is as high as $45 million. Since that is on a daily basis, when one considers the length of time it often takes to receive a returned item, it is easy to see that our bank alone could have a risk exposure of several hundred million dollars on uncollectable items at any one time.

Nevertheless, Bank of America places holds on only a small portion of the checks deposited with us. The decision whether to place a hold is made by the teller accepting the deposit which is subject to review by a branch officer. Generally a hold will be placed only if there is some doubt or uncertainty as to whether it will be paid by the paying bank (for example, we do not know the maker of the check, the dollar amount is large, we cannot verify the legitimacy of the item, etc.), or if the depositor is not well known by the branch or has been unreliable in the past. In practice, it occurs most often in situations where the depositor is a new customer without an established relationship with the bank, in nonrecurring events such as a large dollar deposit on the sale of a home, or where the account has developed a pattern of bad checks in the past.

The length of any hold placed on a deposited check is based on surveys of actual items handled by the Bank; and that length varies according to the electronic routing code which appears on every check. The number of business days a hold is placed on a particular check constitutes the average transit time for items with that routing code to be returned if dishonored during our survey. It is intended to capture a high percentage of the returned items with the recognition that some checks will still be returned after the hold has expired. Generally, checks drawn on out-of-state banks tend to be the ones which most often exceed the average times since they are usually forwarded by U.S. mail rather than by interbank courier.

Bank of America has both a written and oral disclosure policy with regard to placing holds on checks. We plainly disclose our policy on holds in writing when a customer opens an account. Additionally, if funds are to be held, specific disclosure is made to the depositor at the time the deposit is made indicating the date the funds will be available. If the deposit is made by mail, instant deposit, or night depository, the receipt mailed to the customer contains an explanation of what a hold is, why it is placed, and gives the date the funds will be available for the current deposit. To give you an idea of the written disclosures we make, I have submitted several examples for the record. These include an excerpt from our FACTS booklet, which is given to every new customer and describes our hold procedures; the notice on our Instant Deposit envelopes; and the notice mailed to a customer if a hold is placed on a deposit made other than in person. I have also included one of our consumer information reports which we prepared as a guide to checks and checking for our customers.

Because we place holds on some uncollected funds as a protection against loss, Bank of America is in the position of deriving some income from the practice. Income, however, is not the reason for the hold; and because the incidents of placing holds is so low, we have not encountered a significant problem with our customers. In fact, our customers do have the option of having the funds held in an interest-bearing account with interest credited from the date the deposit is made, not from the date the funds are made available. Furthermore, since we do not place holds on most deposits, the customer has immediate use of those funds before we actually collect from the paying bank, and the overall benefit to our customers is far greater than the cost of held checks.

Our policies and procedures are designed to minimize the incidents of holds placed on uncollected funds and to minimize the length of those holds when they are placed, consistent with our need to protect ourselves from the substantial exposure risk encountered.

We believe these policies and procedures go far toward striking a balance between the need to protect the bank from the significant risk involved and providing customers access to their funds expeditiously. However, we recognize that much of the industry as a whole has been critized both for what it actually does and the way it communicates with its customers.

Obviously the placing of holds on certain checks cannot be totally eliminated. Nevertheless, at least two avenues are available for the industry to come to grips with the problems.

The first is to establish a clear understanding of why a bank places holds on uncollected funds. It is important not only for consumers to understand the reasons, but also for the banks themselves to clarify whether they are attempting to protect themselves from losses on returned items, or to reduce float costs. The policies of some banks give no clear indication of which purpose they have. But before a coherent discussion of the issues can take place within the industry banks must determine for themselves the principal reason for placing holds on uncollected funds. Additionally, the reasons and methodology of determining holds should be clearly communicated to a bank's customers. Some banks throughout the country do not make disclosures to their customers either when opening an account or when checks are deposited. If policies are not disclosed, and customers only learn of a hold when checks they have written bounce because the deposited funds the customer assumed were available are, in fact, being withheld, the resulting anger and inconvenience create considerable customer relations problems. This has undoubtedly helped generate substantial consumer complaints on this issue.

The second major avenue is a concerted effort on the part of the industry to make more efficient the processing of return items. As I stated earlier, handling return items is a highly manual and labor intensive task. Several organizations, including the American Bankers Association and the Bank Administration Institute, have identified a number of problems contributing to the delayed processing time for return items. The notification of dishonored items is often slow. The physical return of dishonored items is also very slow, owing to the fact that the items are often returned through the mails to the last endorser rather than to the depositing bank. Additionally, education of bank customers has often been incomplete, not only in terms of explaining the reasons for holds, but also in explaining alternative services for efficient transfers of funds, such as wire transfers.

The issue of delayed funds availability is complex. Nevertheless, it is an issue that can and should be addressed voluntarily by the banking industry in cooperation with the Federal Reserve System. We fully support the Federal Reserve Board's decision last month that banks should be encouraged to adopt disclosures informing customers of their hold policy, thus permitting customers to shop around for appropriate bank services. In California, Bank of America has been instrumental in the efforts of the California Bankers Association and the California Bankers Clearing House Association in adopting measures to encourage banks to examine their customer disclosure policies, their transit hold schedules, and the training of their staff in hold policies. We believe that joint industry and Federal Reserve cooperation in these efforts, while not eliminating entirely the need for placing holds on some deposited checks, will go a long way towards alleviating customer concerns about uncollected funds policies.

Thank you for your time. I will be happy to answer any questions you may have.

The CIRcular™
Consumer Information Report 10

A Guide to Checks and Checking

In this report, you'll learn whom to call if your checks are lost or stolen; what happens when a hold is placed on your account; why two-party checks can be hard to cash; when a check goes "stale"; how to file a stop payment order; and more.

PERSONAL CHECKS Whether your checks are contemporary and colorful or traditionally styled, they always carry your branch and account number on them. That's what makes them "personal." They may also carry your name, address, and telephone number, which more clearly identify you to the person or business to whom you write the check.

Negotiable Order of Withdrawal (NOW) A NOW looks like a personal check and can be used in the same way, but the money it represents actually comes from a special type of savings account. As a practical matter, a NOW account works like a checking account that earns interest.

The information about personal checks presented in this report also applies to NOWs with one exception: because NOW accounts are technically savings accounts, financial institutions will reserve the right to require at least 14 days' advance notice of your intent to withdraw funds. However, this right has rarely been exercised in the past, so it's highly unlikely that it will ever be exercised with NOW accounts. (For further information on NOW accounts and other interest-paying checking plans, see *Interest on Checking: Check It Out*, Report #20 in this series.)

Counter Checks If you forget or run out of your own checks, you can use one of your branch's counter checks, which are provided as a customer convenience. These are preprinted with the branch's name, location, and number, and so can be used only by account holders at your branch. A teller will encode your account number on the check before giving it to you.

Universal Checks You may be able to get a universal check from a bank (not necessarily your own) or a merchant. These are blank check forms on which you fill in the name of your bank, your branch and its address, and your account number. Because you supply all the information, the teller or merchant will take extra precautions to identify you and verify your account.

OTHER TYPES OF CHECKS Though personal checks are versatile, for some purposes you may want to use one of the following types of checks. These are usually considered a good form of payment because they indicate that the funds are actually on account with the issuer. You pay a fee as well as the amount of the check, and you'll be given a receipt.

Cashier's Check You can buy one from any bank and use it in the United States. Typically, cashier's checks are used to make large payments, such as a down payment on a home, but they can also be requested as payment for small items. A bank officer will sign the check.

Domestic Money Order Banks, post offices, and some stores sell these; the maximum face value available varies by outlet. They can be used anywhere in the United States, typically to pay small bills or send money away for mail-order merchandise. You sign the money order as "purchaser."

International Money Order You can buy these for limited amounts, indicated in U.S. dollars, and use them to send money abroad.

Travelers Checks These are generally available in denominations of $10, $20, $50, and $100—sometimes $500 and $1,000. When you buy travelers checks, you'll get a purchase receipt. If your checks are lost or stolen, this receipt will help to speed and simplify refund or replacement of the checks.

At the time you buy your travelers checks you should sign each one; usually you'll be required to sign in the seller's presence. It's important to sign them right away because blank checks, if lost or stolen, can be used by anyone. When you present your checks for cash or payment, you'll be asked to sign again so your signature can be compared. You may also be asked to show identification. (For further information on travelers checks, see *Traveling Money*, Report #19 in this series.)

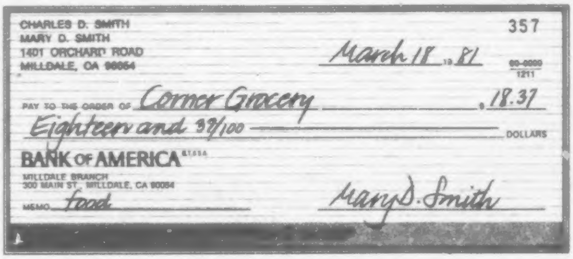
THE FACE OF A CHECK All checks have certain features in common. The following explanations are based on the sample check shown on this page.

March 18, 1981 As of this date—day, month, and year—the check is payable. If there is no date on the check, it is considered current and payable.

A "postdated" check is one dated for some time in the future. If you receive or write a postdated check, the bank may refuse to honor it or may hold it until that date.

A "stale dated" check is usually one that is six months older than the date it carries. Some checks stale date in less time, in which case the stale date is specified on the face of the check in a phrase such as "Not Good after 60 Days." Banks generally will not cash stale dated checks.

Checks drawn on the U.S. Treasury, as Social Security checks are, never stale date. Cashier's, travelers, or other checks drawn on banks' and other institutions' own funds might not stale date either, depending on the institution's policy. Nevertheless, old checks are often difficult to cash.



CHARLES D. SMITH
MARY D. SMITH
1401 ORCHARD ROAD
MILLDALE, CA 90064

357

March 18 19 81

90-0000
1211

PAY TO THE ORDER OF Corner Grocery $ 18.37

Eighteen and 37/100 DOLLARS

BANK OF AMERICA NT&SA
MILLDALE BRANCH
300 MAIN ST., MILLDALE, CA 90064

MEMO food

Mary D. Smith

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Pay to the Order of Either this phrase or one of three others—"Payable to Bearer," "Payable to (name) or Bearer," or "Payable to (name) or Order"—must appear on the check to make it a legally negotiable item.

Corner Grocery The person(s), business, or association to whom the check is written is called the "payee."

$18.37/Eighteen and 37/100 dollars You write the amount of the check in two ways—in numbers and in words—as a precaution against error. If there is a difference between the two, the amount written in words will be paid.

Mary D. Smith Your signature is kept on file at your branch. Always sign your name as you did on the signature card when you opened your account; variations may not be recognized and your check may be returned unpaid.

Milldale Branch The name of your branch (called the "drawee") is on the check so that your account can be located and the check processed and paid.

Cashing Checks

Your branch will cash your check if it's "good"—that is, if it is properly made out, presented by a known or properly identified person, and drawn on an account that contains enough money to cover the check.

A branch may, but is not obligated to, cash checks drawn on another branch of the same bank or on other banks.

IDENTIFICATION Personal acquaintance is the best form of identification. But because it's impossible for all tellers to know every customer who walks into the bank, your identification cards and papers become your introductory credentials. In many cases, you'll be asked to show at least two forms of identification. Most banks, including Bank of America, prefer one of those IDs to carry your picture and/or physical description.

Acceptable Identification Good ID usually consists of a permanent driver's license, a California State Identification Card (issued to non-drivers by the Department of Motor Vehicles), a passport, a courtesy or check guarantee card, a nationally known credit card such as BankAmericard® Visa® or MasterCard™, an employee identification badge or card from a well-known organization, or a military identification card. All must be current.

These are good identification because they all bear your signature, many give a physical description and your birth date and/or show your picture. All have a verifiable number, and many have to be renewed at regular intervals.

Some banks and merchants have incorporated the use of fingerprints, thumbprints, or picture-taking devices into their identification procedures in order to discourage fraud operators from using your ID and trying to cash your checks.

Many banks give courtesy cards to identify customers who have established good banking relationships. Eligibility criteria and card privileges vary from bank to bank.

Unacceptable Identification Most banks and merchants won't accept temporary driver's licenses, Social Security cards, nonlocal or unknown credit cards, library cards, birth certificates, savings passbooks, or checkbooks.

These are unacceptable because they are either too easily obtained or don't firmly establish your identity. Some don't bear your signature. Any card that is expired, altered, or mutilated also will be considered unacceptable ID.

CASHING YOUR PERSONAL CHECK When you cash a check at your branch of Bank of America, the teller will, if he or she isn't personally acquainted with you, leave the window to compare the signature on the check with the one in the bank file. The teller may also leave to verify that there is enough money in the account to cover the check.

At another branch of Bank of America, you will have to show ID unless the teller knows you, and the teller may also call your branch to verify that the check is good.

At a bank where you have no account, you may find it difficult to get your check cashed, depending on the circumstances and the policies of the bank. Many banks, including Bank of America, may charge fees for cashing noncustomers' checks.

No matter at which bank you cash your personal check, always sign it in the teller's presence.

CASHING CHECKS ISSUED TO YOU Checks issued to you by well-known reputable organizations usually present no problem when cashed at your branch, or at another branch of your bank.

Other banks and other branches of your bank may be hesitant to cash checks issued to you by private parties or unfamiliar organizations. This is because tellers may not have sufficient information to verify the check. You always have the option of cashing the check at the branch of the bank on which it's drawn; but if that's not convenient, your own branch is likely to give you the best service.

TWO-PARTY CHECK This is a check that was originally made out to someone else, who in turn signed it over to you. You must endorse it (sign your name on the back) before it can be cashed or deposited.

In theory, a check can be endorsed and negotiated by any number of people. But in practice, you may have difficulty cashing a two-party check or one with several endorsements. One reason for this is that the bank may be required to endorse the check, which is its guarantee that prior endorsements are valid. If the bank can't verify the other signature(s) on the check, it may be unwilling to make the guarantee and so may refuse to cash the check.

YOUR ENDORSEMENT When you endorse a check, you are showing rightful ownership of it. You are also entering into a legally enforceable contract: Your endorsement says you accept responsibility for making the check good—no matter who issued it—should it bounce. (The fact that the bank may later "guarantee" the check by its endorsement does not relieve you of your responsibility.)

- You should endorse a check exactly as your name appears on it. If your name is misspelled, first sign that way and then sign correctly underneath.
- If a check is made out to "(your name) OR (someone else's name)," only *one* endorsement is necessary, though both of you may endorse it.
- If a check is made out to "(your name) AND (someone else's name)," then *both* endorsements must appear on the back of the check. One cannot sign for both, but an exception is made for certain joint tenancy accounts. If the other person has died, you should request that a new check be issued in your name alone. Social Security checks, though, can be specially validated at a local office of the Social Security Administration or Treasury Disbursement.

OTHER ENDORSEMENT FORMS If you wish to sign a check over to someone else, you may endorse it in any of these ways:

1. You can simply sign your name on the back of the check; this is called a blank endorsement. It's important to note, however, that a check with a blank endorsement becomes payable to the holder; if it's lost or stolen, anyone may be able to cash it.

2. You can write "Pay to the order of (the person's name)" and then sign your own name. This is a special endorsement.

3. You can write "Pay to the order of (the person's name) only" and then sign your own name. This restrictive endorsement can also be used if you bank by mail, in which case you'd write "For deposit only" before signing your name.

Depositing Checks

To be sure that your money is deposited into the right account, it's important to fill out the deposit slip clearly and completely.

FILLING OUT A DEPOSIT SLIP Preprinted deposit slips, which come with your order of preprinted checks, simplify this job for you. If you run out of preprinted slips, you may use blank forms provided by the bank. On these, you must fill in your name, branch, and account number.

On Bank of America checks and deposit slips, this information is located in the last ten digits of the encoded numbers on the bottom of the check or deposit slip. On the sample deposit slip shown, the digits are 09991-03456.

The first four numbers, 0999, indicate the branch of Bank of America where your account is maintained. The last six numbers, 1-03456, make up your assigned account number.

Branch and account numbers may be arranged differently on other banks' checks.

How to List Checks On the deposit slip, you must identify checks you are depositing by dollar amount and the ABA number of each. The ABA number is a code, developed by the American Bankers Association, which indicates the bank on which the check is drawn. It normally is in the upper right section of the check, in a form such as

$\frac{90\text{-}0000}{1211}$ or 90-0000/1211.

The ABA number in this case is 90-0000. (The number 1211, indicating the Federal Reserve District in which the bank is located, need not be placed on the deposit slip.)

ENDORSING CHECKS FOR DEPOSIT Each check you deposit into your account should carry your endorsement. A restrictive endorsement, "For deposit only" followed by your account number and your signature, is a good safety measure to use when you bank by mail or endorse checks before you get to the bank.

PARTIAL DEPOSITS If you want to deposit part of a check and take the rest in cash, first endorse the check as usual. On the deposit slip, enter the full amount of the check you're depositing. Record the full amount in the section below marked "subtotal." Enter the amount you want back in cash in the section "less cash returned from deposit." Subtract "less cash" from "subtotal," and enter the difference in the box marked "total deposit."

To show that you have received some cash, you must sign the deposit slip in the teller's presence. At a branch other than your own, you'll be required to show identification.

GET A RECEIPT Always be sure to get a receipt for your deposits. The teller can either record your deposit in the deposit record section of your checkbook, or issue a duplicate deposit slip. If you have deposited checks, the amount indicated on the receipt is subject to verification by the bank. For instance, if one of your deposited checks doesn't clear, or if there's been an error in arithmetic on your deposit slip, the amount actually credited to your account will be different from the amount on your receipt.

Once you have a receipt for your deposit, in most cases you can begin to draw on that money immediately. The exception is when a "hold" is placed on your account.

"HOLD" ON YOUR ACCOUNT A "hold for uncollected funds (UCF)" may be placed for the full amount of a check you deposit if it is (1) written for a sizable amount or an amount that is larger than your account balance; (2) drawn on another bank, branch, or organization; or (3) issued by a person or organization whose reliability isn't known to the bank. The hold means that you can't use the funds until the check has had time to reach the bank on which it is drawn and, if necessary, be returned to the branch where you made your deposit. This process generally takes 3 to 12 business days.

You will be told if a hold has been placed on your account. The teller will note the hold in your deposit record by writing "UCF" and the number of days the hold will be in effect; this will appear next to the date of deposit. If you make a deposit by mail or through an "instant deposit" box in the bank lobby, you will be notified of the hold by return mail.

The hold will be for a specified number of business days (Saturdays, Sundays, and holidays excluded) and for the full amount of the check. After that time, you can begin to draw against the funds. If for some reason the check does not clear, you will be notified.

What Happens If. . .?

Many procedures aren't part of your every-day banking, but you'll want to know about them in case you should need to use them. Here are some of the most important.

LOST CHECKS If you lose any of your personal checks, report this to your bank promptly. A warning will be placed on your account and signatures on incoming checks will be carefully inspected to detect possible forgeries.

If you lose a cashier's check or domestic or international money order—or have reason to believe it was stolen—go to the branch where you bought the item. At Bank of America, you will be asked to sign an affidavit that the item was lost (or stolen) and to have the affidavit notarized. Then, depending on the circumstances, either you will have to sign an indemnity agreement or post an indemnity bond.

An indemnity agreement is your notarized statement that the cashier's check or money order has been reissued to you and that you, not the issuer, will be liable for any loss should the original item later be presented for payment. You sign the agreement and so do two other people who have agreed to be your "sureties"—that is, to fulfill your pledge if you do not.

An indemnity bond also requires that two other people act as your sureties. You buy the bond from an insurance company for a face amount equal to the value of the lost item plus $100 to cover possible costs. Fees are based on the size of the bond and vary by company. The bond should have a term of at least seven years.

As a safety measure, the bank may wait up to 30 days to reissue the lost item.

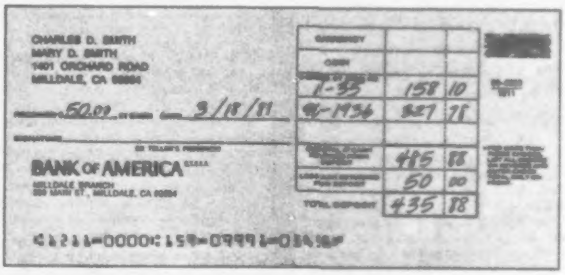
STOLEN CHECKS If you suspect that your checks have been stolen, first make a report to the police in the city or town where the theft took place. Then notify your bank and tell them the time, date, and place the police report was made. A warning will be placed on your account. In some cases, you may be asked to close your account and open a new one under a different number.

FORGERIES As long as you have reported your checks missing or stolen to the proper authorities, you usually will not be held responsible for losses due to forgery. The bank or merchant who accepted the forged check(s) would be charged for the loss.

California law says you have 14 days from receipt of your monthly (or quarterly) statement to review your canceled checks and report a forgery to your bank. If you don't report within this time limit, you may be unable to recover losses from subsequent forgeries.

When you report a forgery to your bank, be prepared to back up your claim. You may be required to furnish your bank with a notarized affidavit of forgery. This document may be used to bring criminal charges against the forger.

STOP PAYMENTS You can order a stop payment on one of your checks if you don't want it paid. Your reason might be that it was lost in the mail or you failed to receive



CHARLES D. SMITH
MARY D. SMITH
1401 ORCHARD ROAD
MILLDALE, CA

50.00 3/18/81

BANK OF AMERICA
MILLDALE BRANCH

CURRENCY		
CASH		
1-35	158	10
90-1956	327	78
	485	88
	50	00
TOTAL DEPOSIT	435	88

1211-0000: 159-09991-03456

merchandise paid for by check. There are two ways to file:

1. You may go to your branch and fill out a stop payment order. The form will ask for specific information about the check—the date it was made payable, the exact amount of the check, to whom it was written, the number of the check, the name of the person who signed the check, and the reason for the stop payment. The bank will verify that the check has not cleared before the stop payment can be placed in effect.

2. You may mail your branch a written request for stop payment. Your letter should include all of the above information about the check and bear your authorized signature. The stop payment will not go into effect until the branch receives your letter and verifies that the check has not yet cleared.

Should the check be presented at the bank for payment while the stop payment is in effect, it will be returned unpaid to the person who presented it. That person will be referred to you for the reason the stop payment was placed.

Under certain circumstances, payment of a check could be enforced even though a stop payment order has been filed. Ask an officer at your bank about the order's limitations.

There is a service charge for filing stop payments, and the order stays in effect for six months. You can renew it if necessary.

REJECTED CHECKS AND OVERDRAFTS If you write a check for more money than you have in your account, the bank may either create an overdraft or reject (bounce) the check.

In the first instance, the bank pays the check and deducts the amount from your account, leaving it with a negative balance. The bank will send you a notice of checks paid in this manner and the amount of the bank's charge. You'll be expected to make a deposit to cover the overdraft and the charge.

In the second instance, the bank rejects the check by returning it unpaid to the person or organization to whom you made it out. You should contact the person or organization immediately to say when you made, or will make, a deposit so that the check can be renegotiated. The bank and many merchants charge for returned checks. If the redeposited check bounces a second time, the bank will again charge you a fee; the merchant may also charge you again.

If you deposit a check that later is rejected by the bank on which it's drawn, the amount of the check will be subtracted from your account balance and the check will be returned to you. The bank may charge you a fee.

Overdraft Protection There are two types of overdraft protection banks may offer to qualified customers. One type involves automatic transfers from your savings account. If you authorize this service, funds will be automatically transferred from your savings account to your checking account in order to cover any overdrafts. Minimum transfer amounts and transfer charges vary among banks.

The other type of overdraft protection service is backed by a credit card or loan account. Qualification requirements differ among banks.

With this service, money is transferred into your checking account when a check you write is for more than your balance. The money that is deposited is charged, up to the limit of your available credit, against either a bank credit card or a loan account opened for this specific purpose. Money that is transferred into your account under this type of plan may be subject to interest charges according to the terms of your agreement. Some plans also charge a fee each time a transfer is made.

Tips to Save Time

When you cash a check, always sign in the teller's presence. If you don't, and the teller isn't personally acquainted with you, chances are you'll have to sign again. The teller must see you sign your name before your identification can be accepted for signature comparison.

When you take cash back from a deposit, always sign the deposit slip in the teller's presence. Remember, this is like cashing part of a check.

Endorse checks for deposit in full before you reach the teller's window.

Always endorse checks just as they are made out to you. If you don't, you may be asked to endorse them again.

Do as much paperwork as you can before you get to the teller's window—fill out deposit slips, including the ABA numbers of any checks, and fill in your personal check except for the signature line.

Your personal check presented for cash can be made payable to "Cash" or "Bearer." If you make it payable to yourself or the bank, you'll have to endorse it on the back. It's safest to write out such a check at the bank.

A little time taken to balance your statement promptly will save a lot of time later if there's an error to be traced. (For help in balancing your checkbook, see Report #1 in this series.) Report irregularities as soon as possible.

Tips to Save Trouble

Treat your checks as you would cash. Keep them as safe and secure as possible.

Don't make changes on the face of a check that's issued to you, and don't take a check that looks as if it has been altered. The bank may refuse to honor such checks.

Avoid carrying checks made out to "Cash" or "Bearer." If they're lost or stolen, there's no control over who can cash them.

For the same reason, never sign your personal check until you have filled in the amount and the payee.

Check all entries the teller makes in your deposit record or duplicate deposit slip to make sure they are legible and correct. If you're taking cash back from the deposit, count your money carefully to see that it's the correct amount. Do both of these things before you leave the teller's window.

Always inspect new check orders for accuracy. Check the spelling of your name, your address, and phone number, and be sure your account number is properly encoded. Any errors should be reported to the bank.

Anytime you have a question about checks or checking procedures, be sure to ask an officer at your bank for an explanation.

Information in this report is effective at the time of printing–February, 1981–and is subject to change.

Prepared by Bank of America, Box 37128, San Francisco, California 94137

BANK OF AMERICA NT&SA • MEMBER FDIC

AD-260 (REV 2-81)

Notice contained on back of instant deposit envelope.

Important

All Instant Deposit items are posted daily and are subject to our verification. Although the deposit is added to your account today, you may not be able to use the funds until the check has cleared. You will be notified if a hold has been placed on any deposited funds. If you have a question about this, a branch officer can help you.

Tear off and keep this stub for your records before sealing the envelope.

Date__________

☐ Checking $______________________

☐ Savings $______________________

☐ Payment $______________________

EXCERPT FROM

"Facts about Bank of America's Checking and Savings Programs"

This booklet is given to each customer opening an account at Bank of America.

HOLDS The bank may place a "hold" for the full amount of a check you deposit if the check is (1) written for a sizable amount or an amount that is larger than your account balance, or (2) drawn on another bank, branch, or organization, or (3) issued by a person or organization whose reliability isn't known to the bank.

When the bank places a hold on a check you've deposited, the deposit is immediately credited to your account. However, you can't use the funds until the check has had time to reach the bank on which it is drawn and, if necessary, be returned to the branch where you made your deposit. This process generally takes 3 to 12 business days.

You will be advised if a hold is placed on your account and when the funds will be available for use.

BANK OF AMERICA

Checking/Savings Hold Notice

BRANCH NAME AND NO. ______ DATE ______

☐ ______ $ ______
CHECKING ACCOUNT NUMBER

☐ ______ $ ______
SAVINGS ACCOUNT NUMBER

Check issued by ______

Dollar amount of check $ ______

If your check is not returned, your funds will be available on ______

Dear Customer:

We have placed a "hold on uncollected funds" (UCF) for the amount of the check deposited to your account.

A "hold" may be placed on a check which is 1) written for a sizable amount or an amount that is larger than your account balance, or 2) drawn on another bank, branch or organization, or 3) issued by a person or organization whose reliability is not known to us.

The deposit is credited immediately to your account. However, you can't use the funds until the check has had time to reach the bank on which it is drawn and be returned to the branch where you made your deposit. This process generally takes 3 to 12 business days.

If you have any questions, please contact your branch.

MISC-209 11-80

BANK OF AMERICA NT&SA · MEMBER FDIC

OLD HANDSHAKE WAY

Senator **CHAFEE**. Well, thank you very much.

Now, Mr. Heron, you've heard the testimony of Ms. Del Bucchia, and it seems to me there is a mammoth bank that still is able to handle this situation in quite a personal way, in practically the old handshake way, as you see from her description. The bank teller examines it, the decision is made, and then goes to the bank manager and then in only certain unusual conditions—a very large amount, they don't know the customer at all, and so forth—and a clear disclosure to the customer of the reasons for the delay. It seems to me that makes a lot of sense.

But from your testimony, I take it your system is unlike that. Am I being harsh on you?

Mr. **HERON**. Mr. Chairman, I don't think you're being harsh and I think our system has some similarities. We do use selective delays and they are based on the routing code on the item. As I suggested, 90 percent of the items are held 3 days or less. I also suggested something that we believe will represent a competitive point of difference in the marketplace, our so-called electronic handshake, that will provide immediate access to deposited items. We believe strongly enough in the competitive point of difference associated with this service feature that we will be actively marketing it.

Senator **CHAFEE**. Now Citicorp has a remittance service which you have embarked on which provides a method, as I understand it, of transferring funds from one bank to another that the smaller banks can use in which their logo actualy goes onto the check but Citicorp handles it. Am I correct in that?

Mr. **HERON**. Yes, Mr. Chairman. We do the processing and servicing for that service.

Senator **CHAFEE**. And one of the advertisements that you stress in connection with this service is the float—official checks, 4.4 days, maximum float, you wire us the funds, the plan offers the opportunity to achieve outstanding returns based on the long 4.4 days float it provides.

Well, now, as I understand, this all clears through a smaller branch you have where—where is that located?

Mr. **HERON**. Mr. Chairman, this service is processed through Buffalo, N.Y. I should point out that's a separate bank, Citibank New York State, which is our upstate New York bank.

Senator **CHAFEE**. Well, suppose I had my account in a small bank in New York City, and I wanted to withdraw that and deposit it in another bank in New York City, I went in and, unbeknownst to me, I deal with my "Bank A," where I'm depositing, and their logo is on the check and they give me a cashier's check but they are using your service which stresses that they've got this 4.4 day float. That might be good for everybody but me, isn't it?

Mr. **HERON**. What would happen, Mr. Chairman, is that item would be received by the depositing bank and then processed through our bank in Buffalo and the hold on that would probably be between 3 and 6 days depending on the item. If that item were deposited at Citibank you would have immediate access to the funds.

Senator CHAFEE. If I deposited the check, I drew it on Bank A and deposited it in a Citibank, I would have immediate access to the funds?

Mr. HERON. Yes; you would have immediate access to the funds. As I pointed out, that is processed through Buffalo, N.Y., and the purpose was not for a remote disbursement but quite the opposite. We have engaged in a policy of broadening our operating base out of the New York metropolitan area and for our upstate bank, Citibank New York State, those operations are conducted in two large processing centers, in Buffalo and in Rochester, N.Y.

Senator CHAFEE. Well, the point that bothers me here, it seems to me—you heard the earlier testimony from Father McEwen and the suggestion from the Fed deploring delays due to using a distant bank as a transfer agent, if you would, and it seems to me Citibank is getting into this very situation.

Here we have a transaction that is entirely within the city of New York. There's no reason when I move from Bank A that I should head toward Citibank because when I draw the check on Bank A its logo—I don't even know Citibank is involved in this. I wouldn't, would I.

Mr. HERON. I think you would, Senator, by an indication on the check.

Senator CHAFEE. Well, I'm an innocent and I pick up a check and it has Bank A's logo on it. Maybe the bank is written on it somewhere, but I wouldn't expect it to have anything to do with Citibank. Why would I? After all, here in your advertisement—you're smart, profit-minded, your logo, meaning Bank A's logo on the check—so it seems to me everything is directed toward me thinking that this is drawn on Bank A.

Mr. HERON. The routing code through Buffalo on an item in New York would approximately add 1 day to it. The purpose of locating these operations in Buffalo was not in fact to add time for clearing but, in fact, to decentralize our operation out of the New York metropolitan area.

I would point out if that item were deposited in an interest bearing checking account, a NOW account, in many organizations around the country—and I certainly know ours—it would recevie interest from the day of deposit before the cash was received by the accepting bank.

Senator CHAFEE. There would still be a hold on it, though?

Mr. HERON. There might still be a hold on that item.

CERTIFIED CHECKS

Senator CHAFEE. Let me ask each of you briefly, excepting the problems that you indicate in your testimony that you face—the problems were raised more by Mr. Heron and Mrs. Del Bucchia rather than Mr. Pickell—let's set those aside and move on now to cashier's checks or certified checks. What's the risk there? What more can a person do? I'm moving from Washington, D.C., from my bank to Wisconsin. I get a certified check. To me it's the best I can do except taking all my cash and putting it into traveler's checks. I then go to Wisconsin, open my account, and I'm stymied. You have a delay. Now why should that be?

I'll start with Mr. Pickell. What more could you want? What more can I do?

Mr. PICKELL. Mr. Chairman, in our system it really isn't a delay. I think the concern raised earlier is in fact the individual who's presenting that certified check for deposit, the individual to whom it is made payable. So you have to be very sure that the individual is the person he purports to be. I can tell you that the identification that he presents does not always prove that the person is who he's supposed to be. People do have falsified identification material.

Senator CHAFEE. Do you get caught on certified checks?

Mr. PICKELL. Beg your pardon?

Senator CHAFEE. Do you get caught on fraud?

Mr. PICKELL. Mr. Chairman, we have not had a problem with certified check fraud ourselves, no.

Senator CHAFEE. Mr. Heron.

Mr. HERON. Mr. Chairman, a certified check could be stolen. There could be theft involved. There frequently are business disputes over a certified check. And we would put a hold on a certified check. The endorsement could be forged. The certification could be forged.

To your question to Mr. Pickell, we did suffer a loss of $150,000 on a certified check in 1980. It was, quite frankly, one of the largest single item losses in dollar magnitude that we have had.

Senator CHAFEE. Well, I think if I walked in with a $150,000 check and you didn't know me, there might be some cause for concern. But suppose I walked in with a $10,000 certified check?

Mr. HERON. Some of the same risks, Senator, would still apply.

Senator CHAFEE. What could I do to plead with you to check and get it expedited? I go to the manager and say, "Please, I need the money."

Mr. HERON. Frequently, Mr. Chariman, the individual would come in and say, "I'm closing on a home this Friday, I'd like to deposit this certified check in my account and I'd like the funds available on Friday." The branch manager would then endeavor to talk to the bank on which the item is written and in fact it would be a very simple, normal transaction.

We were not terribly happy about losing the $150,000. It was on a nonexistent bank. In fact Federal investigators were involved and it was MICR encoded with the U.S. Treasury routing. The dollar magnitudes of some of these items are such that resourceful individuals do try to take advantage of a system where 40 billion checks per year are processed.

Senator CHAFEE. My time is up. Senator Dodd.

Senator DODD. Thank you, Mr. Chairman. Was that "Hot Ralph" that you had there?

Mr. HERON. "Hot Ralph" in fact details some of these procedures in his notorious publication.

Senator DODD. Let me, first of all, thank all three of you for your testimony and really I want to compliment all three of you. To varying degrees, you all have taken a leadership role in trying to expedite and deal with this problem. I think that's to your credit.

RETURNED CHECKS

I wonder if I just might run down a couple questions for each of you. Mr. Pickell, from the Old Stone Bank, you note in your testimony that, "Old Stone's Present policies for crediting customers' accounts may account in part for our favorable experience in checks returned." I wonder if you might explain that a little bit further. What do you see as the connection between your generous crediting policies and the low number of returned checks?

Mr. PICKELL. Senator, in this case I'm talking about the number of checks written on Old Stone Bank that have to be returned to the depositing bank because there were not sufficient funds to cover them. That is different from the statistic that was quoted by the Federal Reserve in terms of checks returned because they could not be paid from the payors bank accounts. In other words, because we give a customer deposit credit quickly, when we try to post checks written against his own account it appears that more funds are then available. Therefore, we would return less checks on his account because he has a greater amount on deposit than might be indicated by a system which would slow down the availability of funds.

Senator DODD. I see. But your percentage of returned checks is almost identical to the average amount found by the Bank Administration who did a study in 1973. How much money do you lose a year because of returned checks?

Mr. PICKELL. Senator, last year we lost $90,000. That was between our business checking and our consumer checking accounts. I would attribute that to the diligence of our people and the sophisticated nature of our online teller system as much as anything. As we have looked at our check losses, we have found that the preponderance of these occur right after an account has been opened and we have put the stress of our operation looking at those accounts during the first month or so.

Senator DODD. New accounts?

Mr. PICKELL. That's correct.

Senator DODD. I wonder if there are any other patterns that have been developed, and I will be asking all three of you this as well—is it out-of-State checks or checks for large amounts—are there certain patterns of problems in addition to the new account that would show up in that $90,000?

Mr. PICKELL. Senator, the checks are not necessarily drawn on out-of-State banks. A number of them are drawn on local banks. The most recent occurance was a situation which involved checks drawn on a local bank. Our new accounts clerks are taught to be particularly diligent when a customer opens an account. The particular situation in question was with a branch in one part of the State where a customer came in to open a new account. When the customer filled out the new account form, it appeared the place he worked was in another part of the State and his home was in yet another part of the State. So they were instantly suspicious as to the nature of that deposit. As a result of the new account clerk's suspicion, we were able to keep the loss to a very minimum.

Senator DODD. What percentage of the $90,000 were new accounts?

Mr. **Pickell**. I would say probably 90 percent of that.

Senator **Dodd**. So new accounts are a particular problem. Is that true, as well, in your experiences?

Mr. **Heron**. New accounts do represent an unusual level of risk. I would not be able to quote a specific number.

Ms. **Del Bucchia**. Yes.

Senator **Dodd**. All three of you, as I recall—does Old Stone pay interest at the moment of deposit?

Mr. **Pickell**. Yes, we do, Senator. We pay to the extent allowed by law and that means that as far as NOW accounts are concerned and our savings accounts, it's whatever rate is stipulated—5.25 percent on the NOW accounts and the stated rate on the particular savings or money market certificate account. We are not permitted to pay interest, by law, on our demand deposit accounts. We would hope that would change over time.

Senator **Dodd**. You wanted to get your licks in, too, and I commend you for that, but I would be—all three of you, I presume engage in investing of these funds where there's a hold, and I presume you're getting the maximum amount available on those funds. As you say, you pay 5.25 percent, while I think I quoted the 1981 figure of the average 3-month T-bill as being over 14 percent. None of you are doing to dispute the fact that the institutions, albeit for legitimate reason for engaging in the practice of holding, do make money as a result of this practice as well; is that correct?

Mr. **Heron**. I think there's revenue associated with it, Senator, and yet the wide difference between 5.25 percent and 14 percent to use your numbers, is less a function of banking practice, than of regulation. One could argue that as a financial institution, we do have the opportunity to get market value on our funds. Unfortunately, the small saver, the individual, the consumer, because of regulation Q, cannot get market value for his funds, which very much deals with the value of float. The value of the float is the difference between the market rate and the regulation Q rate of interest we are allowed to pay to an individual.

Senator **Dodd**. Are you suggesting by that that maybe we ought to—if we were to support deregulation, that in fact that might remove some of the incentive that some may have—I'm not suggesting that you do—some may have for having a hold, for instance, on some of the checks that the chairman has alluded to—cashier's checks and so forth—that presently there doesn't seem to be a significant amount of justication for?

Mr. **Heron**. I think there are two issues. First, clearly, more rapid deregulation on rates would give rise to paying a closer to market rate of funds. Second, there still exists, and it's more than a shadow, fraud in the marketplance, possibly more in our marketplace than others.

Senator **Dodd**. I don't think you'll find any argument on that point up here. I totally understand that. I think if you were to go to the other extreme you would be—I think you might have a hearing here in which we would be questioning whether or not you were being unwise in terms of your policies. I think we're trying to strike some sort of balance.

Mr. **Heron**. I think the real issue was eloquently suggested by Father McEwen. Why disadvantage 99 percent of your customers in this never-ending vigilance on fraud? And that's why we're anxious to build systems, these so-called electronic handshakes, that will give customers immediate access to their funds. The kind of customer we're talking about is the individual who's depositing his paycheck and needs that paycheck for such everyday occurrences as paying the rent, electric bill, and telephone bill.

Senator DODD. Do any of you have any figures on how much you make on the float on an average day of business?

Mr. PICKELL. No.

Ms. DEL BUCCHIA. No.

Mr. HERON. I don't have numbers, either. The real issue, though, is not necessarily how much we make on the float, but what float is unavailable to customers because there's a hold on the money. So I would suggest it's a much smaller dollar number than you might think. I don't think the consumers are looking to their bank of deposit, for immediate access to all their funds.

Senator DODD. I'm driving at the incentive approach. If the dollar amount is significant enough, then the incentive to shorten that period is going to be obviously less.

Mr. HERON. Correct.

Senator DODD. I wonder if you might comment on your Citicard day-to-day card service and what right do you have to secure funds from other bank accounts if the customer's check bounces.

Mr. HERON. This is part of the agreement we enter into with the customer whereby all the balances he has, including the highest yielding instruments we currently can offer, gives us, a version of an electronic handshake. The right offset is there, and if an item comes back to us, ask the customer to make good on that item.

What this does, in a very straightforward fashion, is give the customer as close to market interest on his money as we can get and also immediate access to these funds. Unfortunately, today's convoluted system, a lot of software, necessitated by the inability to offer the customer market rates on a straightforward basis.

Senator DODD. Well, thank you, all three of you, for testifying.

ZERO RISK

Senator CHAFEE. Mr. Heron, the process you described whereby the customer can withdraw his funds without the delay involved up to the extent that he has money market certificates or whatever it might be on deposit, that's nice, but I don't find that so astonishing. It's a zero-risk proposition to the bank, isn't it? I mean, why are you trumpeting it so? And I'm not being sarcastic, but you're perfectly protected, aren't you, under the system you described?

Mr. HERON. Mr. Chairman, you're correct, and yet the issue that was suggested earlier was why disadvantage the 99 percent good, honest, hard-working individuals who we're privileged enough to serve as customers for the 1 percent. Our system accommodates the needs of the 99 percent by giving gives them immediate access to their funds before the bank has the money. In addition, it recognizes these individuals the way my dad was recognized in a bank many, many years ago, which is not part of banking today in a large metropolitan area. It does take advantage of electronics and, furthermore, we do think it will be a competitive point of difference, enough so that we plan to market this service this year.

Senator **Chafee**. The point that bothers me is that a mammoth bank like Bank of America, which indeed is the largest bank in the United States, isn't it——

Ms. **Del Bucchia**. Yes, retail bank.

Senator **Chafee**. First or second largest, is able to handle this matter with considerable expeditiousness and yet the delays that are experienced in other banks—I'm not saying yours, but I'm saying other banks in the country—are these extraordinary ones. As I read, a Government check takes 8 days. It was listed in the testimony Father McEwen gave. And Mrs. Del Bucchia mentioned that they are trying to pressure the California Bankers Association and so forth to follow the examples that they have set, but apparently that's not succeeding based upon the increased number of complaints that are coming about.

So my question to each of you is, if you were sitting here, what would you do about this situation briefly? And you can say, do nothing, say that certainly the banks should give notice—it seems to me the most disturbing thing is so frequently notice isn't given, a person doesn't know. But I'm not going to ask you to answer the question. Why don't we start with Mr. Pickell and don't make the answers too long because we do have another panel.

Mr. **Pickell**. Mr. Chairman, I think the answer is in finding ways to speed up the system, not in trying to add new regulations or requirements on the banks themselves. I believe the Federal Reserve's testimony indicated that is the direction in which they are trying to head and I would commend them for anything they can do in that regard. I would certainly hope that we can move in that arena and not add another regulation to the already increasing number of regulations we presently have to handle.

Senator **Chafee**. OK. What did you get out of the Federal Reserve's testimony?

Mr. **Pickell**. They are trying to speed up the process. I'm not referring to another so-called study, but there are systems that they can implement which we hope would allow a more expeditious system for notifying banks about returned items. To the extent that you can reduce that number down to a bare minimum, I think the banks will be more willing to go forward with relaxed policies.

I would say that our policy as I've already described to you, is quite liberal and I can't believe it would be possible to do much beyond what we have already done.

Senator **Chafee**. Mr. Heron?

Mr. **Heron**. We believe that there's no need for regulation. We think the marketplace can deal with the situation, and we mean that sincerely. If we did not, it would have been foolhardy for us to invest time and effort to develop these electronic systems. We believe there are competitive forces at work and we've seen those forces at work in our marketplace. As I'm sure you're aware, the thrifts in our State got checking powers early in 1976. The way they competed was on price. They basically gave the service away. It was free, which was part of the regulation. Nevertheless, the thrifts established lengthy hold periods which severely inconvenienced many customers, who realized that there's more to a checking account than having a balance. That's why we believe that technology will give us the opportunity to bring a significant point of difference in the marketplace.

Senator **Chafee**. Ms. Del Bucchia?

EDUCATION OF THE CONSUMER

Ms. **Del Bucchia**. Well, I think No. 1, in our eyes, is the education of the consumer. For example, a cashier's check is an example of how the consumer is made aware of the concerns of banks, we would go ahead and find another means of transferring the money if it was urgent. Also, we do feel that the transfer of funds is being improved electronically, but the return of items and the means that they have to travel, through the U.S. mail system and at times to the first endorser causing delays in the return to the paying bank, has got to be changed.

How we can remedy that at this point we do not know because as long as we are using the normal U.S. mail system we are going to run into problems. But if the consumer is educated and banks state a definite position as to how they stand on the delay of funds, I think it will definitely improve the image of the industry and will make customers understand more how banking operations work.

Senator **Dodd**. Just a final point. I don't want to press the point, but it seems to me, Mr. Chairman, that in part, if we were able to get a requirement or at least an understanding of wiring checks, to get those back, that seems to me when you're talking about mortgages and small businesses, as Father McEwen pointed out, that really live on such an edge that a delay of a few days can make a difference between success and failure of a number of industries. I would be curious and I would like to have for the record in the case of the three witnesses—we might be able to get some assessment of exactly what sort of revenues your institutions do collect on an annual basis as a result of the float based on your existing hold practices. I think it might give us some indication of the likelihood of the competitive marketplace resulting in some changes.

I don't say that in a disparaging way at all and I don't expect private institutions to be operating like the Peace Corps, but I do think that is a consideration when looking toward the marketplace as a way of achieving a more expeditious result, and I think that might give us an indication of the likelihood of that occurring on a broader base than it presently does.

And I just want to conclude by saying that I think all three of you represent institutions that seem to me anyway are clearly trying to do things in this area. I don't anticipate that we're going to do anything immediately, but I can see this problem continuing to occur and this Congress or another Congress at some point suggesting something in the area of regulation. I think all of us feel that the burden should be on us to demonstrate a need for regulation, absent an indication in the marketplace that the matter is going to be taken care of otherwise. Thank you.

[The following letter was received for the record:]

OLD STONE BANK

BARRY PICKELL
Senior Vice President
Corporate Affairs

March 16, 1982

Mr. Edward C. Dicks
Senate Committee on Banking, Housing,
and Urban Affairs
Room 5300
Dirksen Senate Office Building
Washington, D. C. 20510

Dear Mr. Dicks:

Enclosed is a corrected copy of the transcript of my remarks before the Consumer Affairs Subcommittee on March 10.

Following my testimony, Senator Dodd requested that I submit additional material for the record concerning the amount of revenue Old Stone Bank receives annually as a result of the investment of float. (See page 76 of the Hearing transcript.) Old Stone Bank actually receives nothing revenuewise from the investment of float because we make funds available to customers on the day following receipt of deposit. This is the earliest possible date that the Bank can obtain credit from local clearing house banks and from our two correspondents which handle all check clearing to other banks within and outside Rhode Island.

If you have any questions concerning the above, please call me.

Sincerely,

Barry Pickell

150 SOUTH MAIN STREET, PROVIDENCE, R.I. 02901 TELEPHONE (401) 278-2513

Senator **Chafee**. As I started out, no one on this committee, I believe, is anxious for regulation, but everybody has been involved with situations, including the customer of your bank, Mr. Herman—perhaps you saw that discussion he had with the president of your bank.

Mr. **Heron**. I did, Mr. Chairman.

Senator **Chafee**. Is Mr. Wriston president or chairman?

Mr. **Heron**. Mr. Wriston is chairman.

Senator **Chafee**. Was that on "Face the Nation" or what was that?

Mr. **Heron**. It was on "Face the Nation," approximately 4 to 6 weeks ago.

Senator **Chafee**. And Mr. Herman had had a long delay. Mr. Wriston said he'd look into it. I'll bet that shook everybody up right down the line, didn't it?

Mr. **Heron**. Further to your point, Senator, Mr. Herman had asked the branch manager what the hold policy was on this item, and it was 6 days. And what happened was that Mr. Herman's employer had decided to pay checks out of another location. So it was a New York City check obstensibly, but in fact it was routed outside the immediate New York City clearinghouse area and the branch manager of Citibank who gave Mr. Herman the response was absolutely correct. There is a phenomenon that as the value of funds increases, corporate cash management occasionally can be aggressively practiced.

Also, apparently Mr. Herman's office was mailing or sending the check to the wrong address which also added some delay.

Senator **Chafee**. Well, let's not pursue that any more. Mr. Herman was upset and that took 11 days to clear.

Mr. **Heron**. It took 11 days, Senator.

Senator **Chafee**. Is that 11 working days or calendar days?

Mr. **Heron**. It's calendar days, and that's why we have occasional disparity as the checks are routed outside of New York City for purposes mentioned earlier with two weekends, including the day of deposit, and you do get 11 days. I'm sure Mr. Herman would have been pleased if he had been receiving interest on that at something close to 14 percent rather than 5.25 percent.

Senator **Chafee**. I don't think Mr. Herman was pleased at any part of the transaction.

All right. Fine. Thank you very much, gentlemen, and Ms. Del Bucchia. We appreciate you coming.

The last two panelists are Mr. Messina, senior vice president, Columbia Savings Loan Association, Woodhaven, N.Y., on behalf of the U.S. League of Savings Associations; and Mr. Charles Arner, president of the First National Bank of St. Paul who's testifying on behalf of the American Bankers Association.

We thank you gentlemen for coming. I know that you have been waiting—I was going to say patiently—perhaps impatiently. We have your statements. If you could summarize your views we would appreciate receiving them, and why don't we start with Mr. Messina.

STATEMENT OF PHILIP MESSINA, SENIOR VICE PRESIDENT, COLUMBIA SAVINGS & LOAN ASSOCIATION, WOODHAVEN, N.Y.; TESTIFYING ON BEHALF OF U.S. LEAGUE OF SAVINGS ASSOCIATIONS

Mr. **Messina**. Good morning. My name is Philip Messina and I am senior vice president of Columbia Savings & Loan Association of New York City, and I will attempt to condense this statement.

I am testifying on behalf of the U.S. League of Savings Associations, and we welcome the opportunity to provide information and some insights.

REGULATION OF HOLD POLICY UNNECESSARY

Because deposit holds are necessary for the protection of the association and are generally exercised reasonably and with concern for the retention of the customer's business, we contend that regulation of financial institutions with regard to deposit hold policy is unnecessary.

A solution regarding delayed access to depositors' funds might be to eliminate as much as possible the need for the customer to physically deposit checks to his accounts—perhaps through the service of electronic direct deposit. Such funds would then be immediately available.

Our conclusions with respect to deposit hold policy are based on a recent survey of the savings associations practices and I'll very briefly summarize our findings.

Savings associations generally attempt to focus their security procedures on situations where risk of loss is greatest and generally seek to avoid inconveniencing customers by not enforcing holds when the risk of loss is minimal. To avoid antagonizing customers, savings associations typically modify their hold policy by waiving holds to certain kinds of checks. They frequently also waive holds for known, established customers. As a result, a typical savings association places a hold on only about one-third of its NOW account deposits.

Furthermore, when a customer check is reported as drawing on held funds, 90 percent of the associations will review the situation before deciding to return the customer's check.

It should be emphasized as well that deposit holds do not affect the interest earned on funds the customer deposits to a NOW account. Most associations pay interest on such funds from the day they are deposited.

With respect to the effect of deposit holds on customers' access to funds, the survey data shows that the number of checks savings associations return unpaid because of drawing on held funds is very low. Detailed analysis of the survey statistics show that 50 percent of the associations serving smaller communities returned no checks because of deposit holds during the entire month of January. Nearly 25 percent of those serving larger metropolitan areas also reported not returning any checks because of deposit holds.

While the effect of holds should be the focus, perhaps some insights on how savings and loans generally establish hold policies might be of interest. The length of hold is determined by the period of time required for the association to be reasonably confident that a deposited check forwarded for collection will not be returned unpaid. Any association can estimate how long it should take for a particular check to be presented and returned if dishonored. However, the actual time taken for checks to be returned is likely to exceed the theoretical clearance times estimated. In fact, a recent 3-week survey of returned items made by my own institution in New York City showed that the number of days between the date the association forwarded the check for collection and the date the returned check was received almost always exceeded the hold period, and usually by a significant number of days.

For example, while the association uses the equivalent of a 7-calendar-day hold for items drawn locally, only 1 percent of the checks returned by local institutions were received within that hold period.

Senator CHAFEE. Well, now, I don't quite understand. If the days were in excess of the hold period, then what happens? The hold continues or the customer has the availability of the funds?

Mr. MESSINA. The item itself that was returned reached us, allowed us to first charge the individual customer's account, after our standard hold period had expired.

Senator CHAFEE. But when the standard hold period expires, the customer has access to the funds?

Mr. MESSINA. That is correct.

Senator CHAFEE. Well, if it takes longer to return them than the hold period, why have the hold period?

Mr. MESSINA. In fact, perhaps the other position would be more reasonable, and that being to extend the hold period.

Senator CHAFEE. Well, one way or the other.

Mr. MESSINA. Indeed. I offer that these results cover approximately the first 3 weeks in February and we're not going to jump on the issue in consideration of the fact that we did have several holidays and so on and so forth during those timeframes. We are still continuing to review the situation to determine whether or not there is any extensive exposure on the part of our institution.

We also had that same experience during that same timeframe with checks drawn outside of the metropolitan area.

Based on survey data reported to the League, it doesn't appear that NOW account customers of S. & L.'s are being disadvantaged by deposit holds. The hold periods which are employed may in fact be inadequate due to the manner in which the check collection system actually deals with the returned items. Any attempt to regulate reduction in length of deposit holds will mean that institutions will be increasingly vulnerable to losses and should such losses occur these costs will obviously be passed along to all customers, most of whom have no responsibility at all for the loss in the first place.

Just to reiterate, perhaps the best emphasis here might be to attempt to encourage business and consumers alike to take fuller advantage of electronic direct deposit systems.

That concludes my statement.

[Complete statement follows:]

Statement of Philip S. Messina

Thank you, Mr. Chairman. My name is Philip S. Messina. I am Senior Vice President and Treasurer of Columbia Savings and Loan Association of New York City and appear today on behalf of the United States League of Savings Associations.[1]

The U.S. League welcomes this opportunity to provide information on the deposit hold policies of savings and loan associations. Our testimony will demonstrate that such policies are necessary to prevent excessive loss to associations offering NOW accounts. It will also demonstrate that deposit hold policies are implemented in such fashion few customers are denied access to funds because of deposit holds. This is demonstrated by the fact that very few customers' checks are returned because they draw on funds still subject to a deposit hold.

Because deposit holds are necessary for the protection of the association and are generally exercised responsibly and with concern for the retention of the customer's business, we contend that regulation of financial institutions with regard to deposit hold policy is unnecessary.

Ultimately, the solution to any concern consumers may have regarding delayed access to deposited funds is to eliminate, as much as possible, the need for the customer to physically deposit checks to his account. This can be accomplished if consumers are able and willing to have checks of all types—payroll, government, dividend, etc.—deposited electronically to their accounts. Such funds would be immediately available. However, the availability and consumer acceptance of electronic direct deposit in the United States currently lags far behind that of other industrialized nations.

These conclusions with respect to deposit hold policy are based on an analysis of savings association practices and experience as summarized in the following sections of this statement.

WHY SAVINGS AND LOAN ASSOCIATIONS USE DEPOSIT HOLDS

A savings and loan association places a hold on a deposited check to reduce the risk that it will incur a loss when honoring customers' checks drawing on these funds. Such a loss can occur when the association pays out funds represented by the deposited check only to find that the check is returned unpaid by the institution on which it is drawn. When this happens, the association incurs a direct loss unless it is reimbursed by the customer.

Savings associations and other financial institutions must be particularly concerned about deliberate attempts of individuals to commit fraud by the practice known as "kiting" or by depositing stolen, forged or bogus checks.

Losses can also be incurred without a customer's initial deliberate attempt to defraud an institution if the customer has withdrawn the funds represented by a deposited check and is then unable or unwilling to reimburse the financial institution when the deposited check is returned unpaid.

As will be demonstrated later, savings associations in using deposit holds generally attempt to focus their security procedures on situations where risk of loss is greatest and seek to avoid inconveniencing customers by not enforcing holds when the risk of loss is minimal. The mitigating effect of such selective policies is apparent by examination of actual statistics for items returned because of drawing on held funds.

THE ACTUAL IMPACT OF DEPOSIT HOLD PRACTICES OF SAVINGS ASSOCIATIONS

Although most savings associations do place holds on checks deposited by customers, the effect is of little consequence to most customers. This is demonstrated by the findings of a survey of 67 savings associations who supplied information about their deposit hold practices with respect to NOW accounts and the effect of these practices on their customers. The survey respondents represented associations ranging in asset size from $50 million to $4 billion and operating in market areas ranging in size from small towns to very large metropolitan areas.

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[1] The U.S. League of Savings Associations has a membership of 4,400 savings and loan associations representing over 99 percent of the assets of the $625 billion savings and loan business. League membership includes all types of associations—Federal and state-chartered, stock and mutual. The principal officers are: Roy Green, Chairman, Jacksonville, FL; Leonard Shane, Vice Chairman, Huntington Beach, CA; Stuart Davis, Legislative Chairman, Beverly Hills, CA; William B. O'Connell, President, Chicago, IL; Arthur Edgeworth, Director, Washington Operations; Glen Troop, Legislative Director; and Phil Gasteyer, Associate Director, Washington Operations. League headquarters are at 111 East Wacker Drive, Chicago, IL 60601. The Washington Office is located at 1709 New York Avenue, N.W., Washington, D.C. 20006. Telephone: (202) 637-8900.

First, it should be emphasized that deposit holds rarely affect the interest earned on funds the customer deposits to a NOW account. Whether or not they place a hold on a deposited check, most savings associations pay interest on such funds from the date they are deposited. Moreover, the customer earns interest on these funds even though the association may have to wait as much as a week to receive the proceeds of the check in a form which allows the association to itself begin earning income on the funds.

Thus, the customer benefits from the savings association practice of paying interest from date of deposit. In doing so, savings associations, in turn, avoid the operating and customer relations problems that would occur if earnings credit were delayed until the association had itself received investable funds from the collection of such deposited checks.

With respect to the effect of deposit holds on customer access to funds, the survey data show that the number of checks savings associations return unpaid because of drawing on held funds is very low. For example, respondents to the survey reported that during January 1982 the frequency with which customer checks were returned for drawing on held funds was as follows:

CUSTOMERS' CHECKS RETURNED FOR DRAWING ON HELD FUNDS PER 100,000 CHECKS PROCESSED

Nature of market area	Average number	Average percent	Number of respondents
Metropolitan (1,000,000+)	66	0.07	13
Metropolitan (100,000 to 1,000,000)	26	.03	31
Small town and suburban	27	.03	14

Detailed analysis of the statistics shows that 50 percent of associations serving smaller communities returned no checks because of deposit holds during the entire month of January. During this period, nearly 25 percent of those serving large metropolitan areas also reported not returning any checks because of deposit holds.

Clearly, the percentage of customer checks returned for drawing on held funds is very low. Furthermore, considering that about 1 percent of all customer checks are returned for all reasons, checks returned for drawing on held funds represent only about 5 percent of the total number returned. Therefore, it is evident that deposit hold policies of savings associations have relatively little effect on the ability of customers to draw on funds deposited to NOW accounts.

Because deposit hold policies are not rigorously enforced, savings associations do incur some losses as a result. During 1981, a period when most survey respondents first began to offer NOW accounts, associations serving large metropolitan areas wrote off an average of approximately $0.71 per NOW account per year because of paying customer checks that drew on uncollected funds. Associations serving metropolitan areas of less than 1,000,000 in population incurred losses averaging $0.67 per NOW account per year. Associations serving small communities incurred considerably smaller losses. Thus, the nature of the market area has a great deal to do with the care that must be exercised in dealing with checks deposited by customers.

Generally, larger losses were associated with relatively liberal hold policies. For example, one large association that, as a policy, did not return any items drawing on held funds, experienced a loss of more than $2.00 per NOW account during 1981 because of paying these items.

DETAILED REVIEW OF DEPOSIT HOLD PRACTICES OF SAVINGS ASSOCIATIONS

While the effect of deposit hold policies is primarily defined by the degree to which the customer is actually denied access to funds, a summary of savings association deposit hold policies may also be of interest. A description of such policies includes how the length of deposit holds is determined, the length of hold applied to various categories of checks, adequacy of deposit holds, the exceptions made in applying holds, the percentage of deposits actually held and the policy for handling a customer check reported as drawing on held funds.

1. HOW THE LENGTH OF DEPOSIT HOLDS IS DETERMINED

The length of deposit hold is determined by the period of time required for the savings association to be reasonably confident that a deposited check forwarded for collection will not be returned unpaid. This period is governed by the number of processing points in the check collection system through which a check must pass in order to be presented to the institution on which it is drawn. These are also the points through which it must pass in reverse order if the check is dishonored by the drawee institution.

An association can estimate how long it should take for a particular class of deposited checks (e.g., checks drawn on local institutions, checks drawn on out-of-state institutions, etc.) to be presented to the drawee institution and returned to the association if dishonored. This estimate can be made making an assumption about the probable route the item will take through the check collection system and also assuming that all institutions handling the item will observe the processing deadlines established by the Uniform Commercial Code (UCC). However, as discussed below, the actual time taken for checks to be returned is likely to exceed the theoretical clearance and return time and therefore some additional time must be allowed.

2. LENGTH OF DEPOSIT HOLDS EMPLOYED BY SAVINGS ASSOCIATIONS

The actual number of processing points through which an item passes for collection and subsequent return is somewhat related to the distance between the savings association where the item was deposited and the institution on which it is drawn. For this reason, savings associations typically classify deposited checks into three groups: those drawn on local institutions, those drawn on institutions outside the local area but within the state and those drawn on institutions out of state. (The exact nature of the market area and check clearing patterns may make it appropriate for an institution to use a somewhat different classification.)

Most associations designate the hold period in terms of calendar days which automatically allows for weekends when checks would normally not be processed. (In the following discussion of hold periods, associations expressing hold periods in business days have been converted to equivalent calendar days.)

The median hold period assessed for various categories of deposited checks by savings associations in different market areas is shown in the following table:

LENGTH OF DEPOSIT HOLD IN CALENDAR DAYS OF MEDIAN ASSOCIATION [1] BY TYPE OF ITEM AND MARKET AREA

Type of item	Metropolitan 1,000,000 plus	Metropolitan 100,000 to 1,000,000	Small town and suburban
Local	4	4	4
Within State, nonlocal	7	7	6
Out of State	9	11	11

[1] Half of the respondents had shorter and half had longer hold periods.

As the table shows, the length of the hold period is related to the distance the item must travel to get to the institution on which it is drawn. The nature of the market area in which the association is located appears to make little difference to the length of hold imposed for various classes of items. The one exception is that associations in large metropolitan areas appear to use shorter holds for out-of-state items. This, perhaps, reflects the fact that such associations have more direct access to the large correspondent banks typically involved in clearing such times.

3. ADEQUACY OF DEPOSIT HOLDS: A CASE STUDY

As stated previously, associations can estimate the hold period required based on the probable flow of the item through the check collection system and the processing deadlines established under the UCC. In actual practice, however, the time required for the item to be presented and returned can significantly exceed this estimate.

A three-week survey of return items made by Columbia Savings and Loan Association in New York City showed that the number of days between the date the association forwarded the check for collection and the date the returned check was received almost always exceeded the hold period, and usually by a significant number of days.

For example, while the association uses the equivalent of a seven-calendar-day hold for items drawn on institutions in metropolitan New York, only 1 percent of checks returned by local institutions were received within the seven-day hold period. About 90 percent took at least 10 days to be returned, 54 percent took at least 13 days, and 10 percent took more than 15 days.

The association had a similar experience with items drawn on institutions outside of the metropolitan area. For these items, the association uses the equivalent of an 11-calendar-day hold. About 10 percent of these return items were received within 11 calendar days. About 60 percent, however, required at least 16 days to be returned and 10 percent took at least 20 days to be received.

Based on this experience, the association could justify lengthening its hold period. To be 90 percent certain that a return item will be received before the hold expires, the association would have to lengthen the hold period on local items from seven days to 15 days while the hold period on out-of-town items would have to be lengthened from 11 days to 20 days.

Informal comments of other savings associations suggest that the experience of Columbia Savings is not unusual. What may be happening is this:

While large-dollar checks being returned are handled expeditiously to avoid being challenged by a claim of late return, return items for small amounts may be handled with less urgency.

Handling of return items is still a costly, time-consuming, manual process. Therefore, resources may first be concentrated on large-dollar items being returned and then applied to any backlog of small items remaining to be handled.

Participants in the check collection system seem to accept this prctice as a realistic way to hold down costs while allowing the system to operate in a reasonably smooth and efficient manner.

4. CONDITIONS UNDER WHICH DEPOSIT HOLDS ARE WAIVED

Savings associations, as they have competed with banks for NOW account customers, have been mindful of the need to avoid antagonizing customers with unreasonable hold policies. Thus, many associations will waive holds under certain conditions. For example, at least two-thirds of associations will waive holds for deposits of government checks, well-recognized payroll checks and cashier's checks. A similar proportion will waive holds on deposits made by established customers. Thus, only a portion of deposits are actually subject to a hold.

5. PERCENTAGE OF DEPOSITS ACTUALLY HELD

For the typical association, only about one-third of deposits are actually held. This reflects the effect of exemptions made for certain types of checks deposited and for established customers. But, even if deposits are held, the actual effect of the deposit hold can only be established based on what happens when a customer's check is reported as drawing on held funds.

6. POLICY FOR HANDLING CHECKS DRAWING ON HOLD FUNDS

More than 90 percent of survey respondents will review the situation when an item is reported as drawing on held funds. The association will look at the number of days before the hold expires, whether the customer has other account relationships and how the customer has handled his checking account. Unless the circumstances are unfavorable, the association is likely to pay the item rather than return it. Less than 10 percent of respondents automatically return checks drawing on held funds.

IMPROVING CUSTOMER FUNDS AVAILABILITY WILL REQUIRE FUNDAMENTAL CHANGES IN THE PAYMENTS SYSTEM RATHER THAN CHANGES IN DEPOSIT HOLD POLICY

Based on the survey data reported above, it does not appear that NOW account customers of savings associations are being disadvantaged by deposit holds. Because savings associations are new entrants into this market and are motivated to increase their market share, most have been careful to avoid antagonizing customers by indiscriminate enforcement of deposit holds. In any event, the hold periods which are employed may, in fact, be inadequate due to the manner in which the check collection system actually deals with return items.

Any attempt to regulate a reduction in length of deposit holds will mean that institutions will be increasingly vulnerable to losses. If institutions incur greater costs because shorter hold periods increase losses due to checks drawing on uncollected funds, these costs will be passed along to all customers, most of whom are not responsible for this increase in costs.

The one change to the payments system that will improve funds availability to consumers without increasing costs is expansion of electronic direct deposit of payroll, dividend and government checks. Such deposits represent immediately available funds to the customer since the institution gets good funds at the same time as it receives the information about the customer's deposit.

Perhaps the solution to eliminating delays in availability of customer funds is to find a way to encourage both business and consumers to accept direct deposit. If direct deposit were more widely accepted, it is possible that both cost and efficiency gains would benefit all.

Senator **Chafee**. Well, thank you very much. I must say, you're a model witness, Mr. Messina. Usually we'll urge witnesses to summarize and they will—not today—but quite frequently they will say yes and then proceed to read every word of their testimony. But you gave an excellent summary of your statement and we appreciate it.

All right. We'll reserve questions and go to Mr. Arner. And, Mr. Arner, if you could summarize, we would appreciate it.

STATEMENT OF CHARLES E. ARNER, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, FIRST NATIONAL BANK OF ST. PAUL; TESTIFYING ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. **Arner**. Mr. Chairman, I will extract about two points from my testimony.

UNIFORM COMMERCIAL CODE

Because check collection is a national activity with much of it interstate in nature, most rules for collection are embodied in the Uniform Commercial Code. The code attempts to determine fairly and equitably the rights and obligations of the parties involved in check collection, including financial institutions and their depositors.

The code considers the practical realities of physical transportation collection as well as the possibilities of fraud. It provides reasonable periods for all parties to make necessary accounting entries and certain rights such as the right to stop or refuse payment are preserved within the code to protect the writer of the check and the integrity of the check writer's deposit account from abuse by either the original recipient or other intervenors such as forgers or others making fraudulent representations.

The basic cause of the practice of delaying availability of customers' funds is relatively clear. There is a mismatch in the time it takes a check to reach the bank on which it's drawn for payment and the time it takes to be returned in the event the check is dishonored. It is manually handled on the way back, recorded, entries made at each point.

The problem of returned checks obviously is not a small one. Because checks generally reach the bank on which they are drawn within 2 or 3 days would take as much as 10 business days to be returned if unpaid, most banks have uncollected checks amounting to well over their total capital accounts outstanding at any one time.

Mr. Chairman, the First National Bank of St. Paul has total assets of $3 billion, deposits, savings and checking of $1.2 billion with capital accounts of approximately $200 million. The average checks in process of collection over the past 3 months totaled $277 million, a daily average that peaks at 200 percent of that total on given days.

Within the industry, the approach to funds availability varies based on bank experience, location, customer profile. The majority impose delays on an exception basis with the delay usually being 5 days for local checks and 10 days for out-of-town checks.

Senator CHAFEE. These days we're receiving, are these calendar days?

Mr. ARNER. These are working days.

Senator CHAFEE. These are business days?

Mr. ARNER. Yes. For the record, I have a copy of our rules and regulations in which our policy on the availability of funds is described in this plain English document.

Some banks with long-established depositor bases may never impose delays. Unfortunately, many of these lattermost banks often have to end that no-delay policy after being victimized by check kiting or other embezzlement schemes. I might add that check losses at First National Bank of St. Paul in 1981 were $50,000. You may consider that small. In January 1982, one loss was $198,000. It's unpredictable.

We have not neglected our responsibilities to maintain and improve the system for check collection and we are trying to expedite the return process to something closely approximating the rapid presentation process. I'm happy to report that the first step in a two-part plan addressing the basic problem of unreadable endorsement that cause delays in the return process has been completed. In separate research, our association has studied and devised a pilot project operating since April 1981 to study the effects of checks storage techniques at the bank of deposit rather than the outmoded practices of clearing the items physically and returning them to the customer. The pilot has been well received by corporate depositors. An interesting sidelight to the research is that by keeping the check itself at the bank of deposit and electronically clearing the funds, the return process in the event of dishonor is just as efficient as the original clearing. This research continues to be supported both by our association and by the members participating directly in the research.

I would like to conclude by saying that we in the commercial banking industry are service organizations, are willing to accept risks. Our biggest problem is to identify the people that walk into the lobby of the bank. The teller's world is an entirely different world, facing those people who are presenting you with checks day to day and they are unknown.

That concludes my testimony.

[Complete statement follows:]

STATEMENT OF THE
AMERICAN BANKERS ASSOCIATION
BEFORE THE
SUBCOMMITTEE ON CONSUMER AFFAIRS
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
ON THE ISSUE OF
COLLECTION AND AVAILABILITY OF FUNDS

March 10, 1982

Mr. Chairman and members of the Subcommittee, I am Charles Arner, Chairman and Chief Executive Officer of The First National Bank of St. Paul. I am testifying today in my capacity as a member of the Association's Payments System Policy Board. Additionally, I served as Chairman of a joint ABA-Federal Reserve Task Force which addressed the issue of funds availability in late 1978 and early 1979. Our Association consists of more than 13,000 full service banks, over 90% of the nation's banking community.

Thank you, Mr. Chairman, for this opportunity to put into the public record our Association's views on this matter of the collection and availability of funds to financial institutions and their customers. My testimony will attempt to explain in plain language the technical, legal and practical environments in which financial institutions and their customers participate in the nation's largest payments system.

More than ever, the forces of competition and technology are reshaping the public understanding of the payments system and how individuals and businesses invest and collect their funds. The broad competitive marketplace includes over 40,000 depository institutions, of which some 14,500 are full service banks. In addition, there are many non-depository institutions competing for individual savings and transaction balances. In the past few years, the Congress has expanded the competitive arena for deposit dollars through the enactment of such legislation as the Monetary Control and Deregulation Act of 1980. The competitive marketplace has also created such phenomena as money market mutual funds and other instruments that closely resemble traditional savings and checking accounts in many respects.

Into this competitive environment we have seen the introduction of new technology in the form of electronic banking services that permit more convenient access to balances and more rapid crediting and collection of obligations by both individual citizens and businesses. Automated teller machines allow ready access to collected balances in customer accounts in 25,000 locations across the country. Automated clearing houses provide, among other services, the immediate and safe deposit of some 200 million government payments and 120 million credit transfers within the private sector annually. These and other new services are finally beginning to have an impact on the enormous volume of checks that circulate physically among businesses, citizens and government agencies.

Even with the progress that has been made towards more efficient and productive methods, however, the annual volume of checks continues to grow at a rate of five percent per year. The volume of checks and check-like instruments written in the United States each year is now estimated to exceed 35 billion items annually. This paper avalanche is physically collected through the cooperative efforts of financial institutions across the country, and relies heavily on the resources of the Federal Reserve System and privately operated local clearing houses.

Because it is a national activity with much of it interstate in nature, most rules for collection are embodied in the Uniform Commercial Code. The Code attempts to determine fairly and equitably the rights and obligations of the parties involved in check collection, including financial institutions and their depositors.

The Code considers the practical realities of physical transportation and collection, as well as the realities of inadvertent errors, frauds, forgeries, and other forms of theft. It also provides reasonable periods for all parties to make necessary accounting entries for the items. Certain rights, such as the right to stop or refuse payment, are preserved within the Code to protect the writer of the check and the integrity of the check writer's deposit account from abuse by either the original recipient or other intervenors, such as forgers or others making fraudulent representations. In effect, the Code regards both banks and their customers as having both a right of return and a right to be protected from fraud or negligence in the collection process so long as all parties are timely in discharging their responsibilities under the law.

Financial institutions, in keeping with their regulators' concerns for appropriate levels of business risk in relationship to the obligations of the Uniform Commercial Code, make a distinction between those funds that have been finally collected and have no further risk associated with them and those funds over which the check writer still retains rights of return under the Code. In the interests of reduced cost to the depositor and lower operating expense to the financial institution, bookkeeping transactions to the customer's account are made as soon as possible after the deposit is accepted for collection as is feasible to the institution. In many cases, the credit is virtually immediate.

Savings and time accounts generally have rather infrequent withdrawals and the term of the deposit, in most cases, far exceeds the period of collection risk. On the other hand, payment accounts, such as the traditional checking accounts and the newer negotiable order of withdrawal accounts, because of their more frequent withdrawal and deposit transactions, have closer intervals between deposit and subsequent withdrawal. Once a customer has established an account pattern -- the deposit of the weekly pay check, the regular pattern of debits for housing, utilities and similar obligations -- most transactions can be accommodated with minimal collection risk to the financial institution. Occasionally, an out of the ordinary transaction appears that breaks the established pattern for the account.

At such times, especially if the check originates from some distance away, the institution often reminds the customer of the collection risk inherent in the Uniform Code. This is usually a short reminder such as a requirement to delay withdrawal of funds for several days to insure that the original writer of the check in fact has not withheld payment for some technical reason or otherwise asserted his rights under the Code to refuse payment on the item.

The basic cause of the practice of delaying availability of customer funds is, therefore, relatively clear: there is a mismatch in the time it takes a check to reach the bank on which it is drawn for payment, and the time it takes to be returned in the event the check is dishonored. Because banks do not have any way of determining in advance whether a check drawn on the account of someone other than their customers will be paid when presented, banks have limited options in ensuring that they do not suffer losses on checks accepted for deposit. They can accept a guarantee or credit agreement from their depositors making the depositor liable for unpaid, deposited checks; they can delay availability of funds for depositors until sufficient time has elapsed for a check to be returned if unpaid; or they can review customer accounts to ensure that those checks deposited for immediate credit reflect the pattern or practice of dealings that banks have had with their customers. Most banks appear to follow this last course, with checks deposited that are drawn from beyond their local area or are not consistent with the previous pattern a customer has evinced receiving special treatment by having their availability delayed or by some other means.

The problem of returned checks is not a small one. Because checks generally reach the bank on which they are drawn within 2 or 3 days, but take as much as 10 business days to be returned if unpaid, most banks may have uncollected checks amounting to well over their total capital accounts outstanding at any one time. It can easily be seen that if only a small percentage of these checks were returned unpaid and banks had no means of recovering the funds represented thereby, the total net worth of the banking industry could quickly be exhausted. That is why bank examiners, as well as sound banking practice, insist on procedures to assure repayment of unpaid checks.

Within the industry, the approach to funds availability varies based on bank experience, location, and customer profile. Some banks impose across-the-board delays of, usually, 2-3 days. The majority impose delays on an exception basis with the delay usually being 5 days for local checks and 10 for out-of-town checks. Some few banks with long-established depositor bases may never impose delays. Unfortunately, many of these lattermost banks often have to end a no-delay policy after being victimized by a check kiting or other embezzlement scheme.

The system is by no means perfect. The Code has become intricate and voluminous over the years. A committee of respected attorneys has been at work for some years to simplify the maze of rights and obligations inherent in the payments Code. Our Association supports and contributes to this effort. I mentioned earlier the extensive efforts of financial institutions to improve payment services through innovative use of technology in devising more efficient electronic transfers of funds. Our Association supports and encourages these efforts as well.

Nor have we neglected our responsibilities to maintain and improve the system of check collection that has served us and our depositors for so many years. We have attached for the record a copy of a final report of a joint committee we established with the Federal Reserve some time ago addressing this very issue (Exhibit A). Basically the report recommended the following:

1. That the Board of Governors of the Federal Reserve System recommend that each bank have a written policy on delayed funds availability that is consistent with task force recommendations.
2. That the Board of Governors of the Federal Reserve System not attempt to define specific times associated with the length of allowable delay. Rather, the delayed funds availability imposed by a bank should be defensible, on the basis of that bank's check collection records, and at a maximum should not exceed the normally expected clearing and return period.
3. That the Board of Governors of the Federal Reserve System inform the Chief Executive Officer of each bank by letter of its position on recommendations one and two including a copy of this report as background.
4. That the Board of Governors of the Federal Reserve System consider requiring that each bank have a written policy on delayed funds availability and disclose the provisions of that policy to each affected customer.
5. That the Board of Governors of the Federal Reserve System communicate the work of the task force and the actions the Board has taken or is considering taking to other Federal or financial institution regulators. The task force believes that survey and

study work with a goal of determining the delayed funds availability practices of all financial institutions is necessary. Based on the results of such surveys the other financial institution regulators may find it desirable to develop recommendations similar to those contained in this report.

6. That the American Bankers Association undertake to expedite necessary action to accelerate the return of dishonored items.

7. That the American Bankers Association accept responsibility to coordinate development, introduction and implementation of a new financial service, satisfactory to all segments of the financial industry, to meet the needs of the "new customer." This service should, at a minimum, provide a customer the means to satisfy identity requirements at a new bank, as well as provide the means to authenticate funds on deposit at another bank and to arrange for immediate or very limited delayed funds availability from the new bank.

We filed another white paper with the Fed staff on this issue in July of 1980 (Exhibit B). This paper deals with issues of safety and soundness of financial institutions and reflects the concerns of bank auditors and Federal bank examiners on the issue.

In addition to these efforts we made with the Federal Reserve to attempt to expand the emphasis on more timely collection of checks and more timely returns, we pursued our own course of action within the environment of the American National Standards Institute (ANSI). We are attempting a solution to the growing problem of returned checks. Mr. Chairman, we addressed this problem in much the same way that we successfully accelerated the processing of checks several years ago. We brought together the best experts we could find in the recognized format of ANSI. A two-step process was recommended in order to automate the return of checks. We are trying to expedite the return process to something closely approximating the rapid presentation process we have developed over the years through the invention of a system of routing numbers on checks and magnetic ink character recognition to allow machine processing. (I should note, Mr. Chairman, that the commitee on financial services within ANSI is funded entirely by our Association and staffed by our Association on a continuing basis and is open to all interested parties. You may wish to review the excellent representation from the financial services community on the committee that is addressing this issue.)

I am happy to report that the first step in the two-part plan -- addressing the basic problem of unreadable endorsements that cause delays in the return process -- has been completed, published and circulated by ANSI. In addition, our Association's Check Processing Committee has circulated the new standard to local clearing houses and formed a new committee to work out the details of a more automated and efficient return process for checks.

In separate research our Association has studied and devised a pilot project operating since April of 1981 to study the effects of check storage techniques at the bank of deposit rather than the outmoded practice of clearing the items physically and returning them to the customer. The pilot has been well received by corporate depositors. An interesting sidelight to the research is that by keeping the check itself at the bank of deposit and electronically clearing the funds, the return process in the event of dishonor is just as efficient as the original clearing. This research also continues to be supported both by our Association and by the members participating directly in the research.

That concludes my prepared statement, Mr. Chairman. We are encouraged by your concern for finding solutions to these difficulties in the time worn check collection system that has served banks and their customers so well over the years. We agree that the system requires creative innovations to serve financial institutions and their customers in the future. We welcome any questions from you and your Subcommittee.

Exhibit A

FINAL REPORT AND RECOMMENDATIONS OF THE DELAYED FUNDS AVAILABILITY TASK FORCE

February 16, 1979

Recommendations

In completion of its assignment to evaluate delayed funds availability practices and suggest means of resolving any specific problems that are identified the Delayed Funds Availability Task Force recommends the following actions.

1. That the Board of Governors of the Federal Reserve System recommend that each bank have a written policy on delayed funds availability that is consistent with task force recommendations.
2. That the Board of Governors of the Federal Reserve System not attempt to define specific times associated with the length of allowable delay. Rather, the delayed funds availability imposed by a bank should be defensible, on the basis of that bank's check collection records, and at a maximum should not exceed the normally expected clearing and return period.
3. That the Board of Governors of the Federal Reserve System inform the Chief Executive Officer of each bank by letter of its position on recommendations one and two including a copy of this report as background.
4. That the Board of Governors of the Federal Reserve System consider requiring that each bank have a written policy on delayed funds availability and disclose the provisions of that policy to each affected customer.
5. That the Board of Governors of the Federal Reserve System communicate the work of the task force and the actions the

Board has taken or is considering taking to other Federal or financial institution regulators. The task force believes that survey and study work with a goal of determining the delayed funds availability practices of all financial institutions is necessary. Based on the results of such surveys the other financial institution regulators may find it desirable to develop recommendations similar to those contained in this report. Task force members will make themselves available individually or collectively, as requested, for such additional study efforts as are deemed warranted.

6. That the American Bankers Association undertake to expedite necessary action to accelerate the return of dishonored items.
7. That the American Bankers Association accept responsibility to coordinate development, introduction and implementation of a new financial service, satisfactory to all segments of the financial industry, to meet the needs of the "new customer." This service should, at a minimum, provide a customer the means to satisfy identity requirements at a new bank, as well as provide the means to authenticate funds on deposit at another bank and to arrange for immediate or very limited delayed funds availability from the new bank.

Background

For some time banks have been faced with the decision of when to release funds from deposit accounts represented by checks deposited to those accounts. The problem arises from the fact that a check has no investable cash value, it must be collected from a paying financial institution to convert it into useable funds. Because the process of "collecting" a check involves physically transporting the check from the bank where it is first deposited to the paying bank there is always some delay between deposit and check payment. The time normally required for transportation to the paying bank and return of dishonored items is referred to in this report as the "collection period."

If a bank allows its customer to withdraw cash — or cashes a check drawn on another bank -- it is in effect making a non-interest bearing loan for the time period required to collect the check. Conversely, if a bank restricts its customer's ability to withdraw funds for a period longer than the collection period the customer may be unfairly denied the use of these funds during some portion of that extended period.

As a result of a highly competitive environment and the difficulty of placing a "hold" on funds in consumer accounts, banks have not always restricted customer withdrawals nor do all banks do so today. Recently, however, an increasing number of complaints have been registered by consumers concerning the withholding of funds for extended periods. For convenience this practice of withholding funds, represented by checks deposited into accounts at financial institutions, is referred to in this report as delayed funds availability. In light of its dual roles as regulator with responsibility for consumer affairs in the financial industry and as operator of check collection facilities that handle about 40% of the nation's check clearing, the Federal Reserve formed the Delayed Funds Availability Task Force in September 1978. The American Bankers Association has participated in the work of the task force with staff and bank operating management representatives. The purpose of the Task Force has been to evaluate delayed funds availability practices and suggest means of resolving any specific problems that are identified.

The Consumer Affairs Division of the Board of Governors of the Federal Reserve System conducted a survey of nearly 1,000 banks in early 1978 to develop information on several areas of consumer concern evidenced by complaints received. Delayed funds availability was among those areas surveyed. This survey is available from the Board of Governors of the Federal Reserve System.

In forming the Delayed Funds Availability Task Force the Federal Reserve utilized a small working group with representation from banks of diverse size and geographic location. To minimize the burden on the financial industry the task force was encouraged to use the data from the existing Board of Governors survey and the knowledge and experience of task force members in lieu of a special survey for this purpose alone.

Based on the Board's survey finding that about half the banks surveyed have formal policies establishing delays on all or certain checks received in deposits and the observations of banker task force members that banks without formal policies probably practice delayed funds availability in certain cases; the task force concluded that delayed funds availability is a widely employed and common banking practice. Bankers are, however, quick to defend the need for this practice. First, they say there are delays associated with physically collecting checks and second, there are also risks associated with allowing customers to withdraw funds before the bank can reasonably believe the checks will not be returned. In addition, there would no doubt be bank examiner concern with a practice of always allowing withdrawal before collection if the sums were large or losses frequent.

There are some inherent characteristics of the present check collection system which dramatically affect a bank's ability to be totally responsive to a customer holding a check who needs or desires to convert it rapidly to cash. Today's check collection system is operated on the legal basis established by the Uniform Commercial Code as adopted by each of the 50 states and for those checks collected through the Federal Reserve by the Federal Reserve's Regulation J.

Checks are encoded with machine readable magnetic ink enabling high speed sorting by collecting banks (banks which receive the checks in deposits and other banks including the Federal Reserve which act as intermediaries in the collection process) and by paying banks (banks on which the checks are drawn or through which drafts are payable). As the checks move through collecting banks each bank grants the preceeding bank "provisional credit" subject to revocation if the check is returned. The paying bank is allowed, in most instances, to return unpaid checks up to midnight of the day after the day of receipt from a collecting bank.

A 1973 1/ study found that 0.67% of all checks processed are returned. Of those, 72% were returned because of insufficient funds on deposit to pay the checks. In order of decreasing incidence the following causes for return checks were also noted: missing endorsement 6%, account closed 4%, payment stopped 3%, irregular signature 2%, drawn on unlocatable funds 1%, and other causes 12%. That study also noted that "actual losses incurred from the processing of return items [to be distinguished from the cost of processing those items] is reasonably small when compared to the total number of return items processed." It projected total losses written off by banks due to uncollectable checks in 1973 as being $5 million, or approximately $20 for every 100,000 checks processed. 2/

1/ The Impact of Exception Items on the Check Collection System, 1974, Bank Administration Institute, p. 25.

2/ Id., p. 26.

If a check is returned it must be returned to each collecting bank that handled it in exact reverse sequence as established by endorsements on the back of the check. Although collecting banks use high speed computer sorting equipment to speed the forward movement of checks for collection the return movement is slowed significantly by the need to manually read all endorsements and route the check sequentially back through each collecting banks until it ultimately reaches the bank of first deposit. For example, a check requiring one day in the forward collection process may require until midnight the day after receipt to begin the return movement and will require two additional days for completion of the return process for a minimum of five sequential business days or a longer number of calendar days if a holiday or weekend is involved.

In the example referred to above the bank of first deposit would have "provisional credit" one day after entering the check for collection. It can use the "provisional credit" to meet reserve requirements or otherwise invest these funds but it must be prepared to give up the "provisional credit" immediately if the check is returned. It is important to recognize that a returned check is the only reliable feedback provided to the bank of first deposit that the check has not or cannot be paid by the paying bank.

Banks that allow immediate withdrawal of funds on deposits of checks are extending interest free credit to their customers and are accepting the risk of recovering the withdrawn funds from those customers. Those banks that delay availability of funds to their customers are neither extending credit nor accepting risk for the period the delay is imposed.

There have been few complaints with respect to delaying availability of funds for the period of the forward movement of a check to the point in time where the bank of first deposit receives "provisional credit." Regardless of the inconvenience most consumers and bankers seem to agree it is reasonable to allow time for the physical movement of the check in the collection process.

Disagreement, discontent, complaint and misunderstanding are frequently observed with respect to any additional time delays, beyond the time of "provisional credit," on funds availability imposed by a bank to allow for return. The decision to delay funds availability is a business decision regarding the risk of recovering funds for returned checks from a bank's customers in general or specific customers if imposed selectively.

Banker task force members report a continuing incidence of criminal activities involving checks including check kiting and negotiating stolen or counterfeit checks. As a result banks have adopted risk management programs to protect themselves from these activities. In addition, there are customers who appear to be financially irresponsible as evidenced by frequent or unresolved overdrafts. Delaying funds availability is one means a bank may employ to limit its risks associated with criminal activities and avoid the unpleasant if not impossible task of obtaining restitution of funds for returned checks from financially irresponsible customers.

The task force has concluded that banks are alert to detect criminal activities and financially irresponsible customers as quickly as possible. After an account has been established for a period of 30 to 90 days it should be reasonable to expect a bank to have identified a high risk customer and initiate appropriate action. As a result of this observation, the task force has identified the need to separately consider delayed funds availability problems with respect to "new customers" and "established customers."

New Customers

At the time of new account opening a customer may be changing local banking relationships, opening an account for the first time, establishing an additional banking relationship or moving into a new area. Frequently, the new customer and most particularly the customer moving to a new area will need some cash immediately and will encounter, sometimes for the first time, delayed funds availability.

From the consumer point of view few circumstances are more frustrating than having closed an account in one bank and with an official bank check in hand attempt to open an account in a different bank, be told that funds cannot be withdrawn from the new account for a period of time. After all, the consumer knows the money has been set aside at the former bank and that the check will be honored.

The new bank, however, has no assured way of knowing the customer is the same person named on the check, that the check has not been stolen or counterfeit or that the check will be paid. Since there is no universal and risk free means of identification available in the United States, banks frequently require a "satisfactory" account relationship over a period of time as the means of customer identification. The United States Treasury recognizes and calls attention to the identification problem when it provides the following "Identification Procedure" printed on the back of each of its checks: "When cashing this check for the individual payee, you should require full identification and endorsement in your presence, as claims against endorsers may otherwise result."

Normally, the customer has little knowledge of these problems and has not taken any precautionary measures such as obtaining cash or traveller's checks to weather the delayed funds availability period. Presently, there are very limited means within the banking industry to serve the immediate cash needs of the "new customer" and the most common advice, to use an official bank check as a secure means to transfer funds from an account in another bank, will frequently frustrate immediate cash needs.

As a result of these factors the task force concluded that a new banking service should be developed that would overcome the new customer identification problem. The identification problem listed above applies equally to checks and electronic funds transfers such as wire transfers or automated clearinghouse credit transfers. Releasing funds to a new and unknown bank customer can be risky business.

In order to develop the specifications of a new banking service that could overcome new customer identification problems the task force has requested the assistance of the American Bankers Association. Minimum requirements for the service would be to provide the means for a customer to satisfy identity requirements at a new bank as well as the means to authenticate funds on deposit at another bank, and to arrange for little or no delayed funds availability at the new bank.

Established Customers

All task force members agree that credit worthy, financially responsible, established bank customers should be granted the earliest possible availability of funds for the checks they might deposit. They also agree that there may be valid exceptions for unusually large dollar value checks or situations where the financial responsibility of a customer appears to be deteriorating.

In this regard, the task force believes that any policies, rules or regulations governing delayed funds availability should encourage banks to identify and protect themselves and their depositors against crime and risk associated with financially irresponsible individuals. Banks should retain the flexibility to provide established, financially responsible customers with funds availability on a schedule at least equal to the receipt of "provisional credit" by the bank without extending similar funds availabilaty in situations that may involve crime or financially irresponsible individuals.

Along these lines the task force has prepared a draft letter that could be sent to the Chief Executive Officer of each bank by the Board of Governors of the Federal Reserve System asking that the bank's delayed availability policies and practices be reviewed.

Delayed availability practices or policies should be related to the bank's actual check collection and return experience. The task force believes the provisions of the banks' delayed availability policy should be given to the public on request and disclosed to affected bank customers.

Sample disclosure statements have been developed and are enclosed in Attachment I. Sample bank policy statements have been developed and are enclosed in Attachment II.

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ATTACHMENT I

Sample Disclosure Statements

The banker members of the task force were asked to prepare sample delayed funds availability policy disclosure statements. One of these statements could be used to inform customers and prospective customers of the banks policy on delayed funds availability.

SAMPLE A

Disclosure Statement on Delayed Funds Availability Policy

Checks deposited to established checking and savings accounts at (bank name) are normally available for withdrawal within ( ) business days. An established account is one which has been opened and active for at least 90 days without overdrafts, NSF checks, or other undesirable experience.

Certain circumstances may cause checks to be held for longer periods. This is more likely to occur with large checks or drafts drawn on out-of-area or foreign banks. The period for which these funds are held will be governed by the bank's previous experience in collecting similar items.

Any of the bank's officers will be happy to provide specific information about the availability of any check or draft you wish to deposit. Should you anticipate an immediate use of funds deposited, we encourage you to discuss this need with an officer to avoid any possible inconvenience.

This policy represents our best effort to achieve a reasonable balance between our desire to provide prompt, convenient banking services and our responsibility to protect the funds of our depositors and the investment of our stockholders.

SAMPLE B

Disclosure Statement on Delayed Funds Availability Policy

_________________ Bank does not normally restrict the withdrawal of funds deposited to established checking or savings accounts for longer than three business days. An established account is an account which has been active and satisfactory for 90 days or longer.

Under certain circumstances availability for large items deposited to accounts; drafts, checks or foreign banks, and certain other types of deposits may be withheld for longer periods of time depending on actual prior experience.

Any officer of the bank will be glad to provide availability schedules for particular types of items deposited. You are encouraged to inquire if you have an immediate need for deposited funds which may be unusual for your account.

ATTACHMENT II

Sample Bank Policy Statements

The banker members of the task force were asked to prepare sample delayed funds availability policy statements they would propose to their bank's management. There are different approaches exemplified in these samples which the task force members believe can be used with satisfactory results.

DELAYED FUNDS AVAILABILITY POLICY

The policy of this bank is to provide the earliest availability of funds on deposited checks as is realistic. However, we reserve the right to place restrictions with respect to the withdrawal of such funds, for a period sufficient to receive notification that a check has been dishonored. Any such delay of availability will not exceed the normal time required for notice of dishonor.

Restrictions or holds on the withdrawal of funds shall be limited to a maximum of ___ working days. They may be placed on cash back or split deposits and deposits to new accounts, provided the customer is informed of the restriction, the reason for its initiation and the time duration. Checks deposited to established accounts (___ days old) will normally be accepted without restriction.

Provisions of this policy will be included in the written material given to depositors at the time an account is opened.

Questions regarding this policy or specific transactions may be discussed with a personal banker.

Background

Delayed Funds Availability is the common practice of restricting withdrawal of funds from savings and checking accounts for a period of time to allow for the presentment and possible return of checks deposited in these accounts. The practice protects the bank from risk of loss in the event deposited checks prove uncollectible.

Restrictions on withdrawal (holds) of funds are employed under one or more of the following conditions:

1. At the time a new account is opened with the initial deposit consisting of not-on-us check(s).
2. At the time not-on-us check(s) are accepted as a deposit to an existing account.
3. At the time a split or cash back deposit of not-on-us check(s) is made to an existing account.

The key factors in determining the need for restriction on withdrawals are:

1. Identity of the depositor.
2. Authenticity of the check and the probability of sufficient funds available upon presentment.
3. The bank's recourse in the event of a dishonor upon presentment of the check(s).

NON
P.O.D. BANK

BANK POLICY OF DELAYED FUNDS AVAILABILITY

INTRODUCTION

The types of accounts covered in this bank policy are Demand and Savings accounts that are termed either "Business" or "Individual". Proper resolutions and signatures must be on file at the bank. Bank account relationships must be X (90 or more) days.

This policy is based on the total bank relationships the account holder has established with the bank rather than on the individual account level. Considerations involved are the Line of Credit, Check Guarantee, Savings Transfer to cover O.D. services, as well as other banking account relationships in the form of time deposits, loans, trust, etc.

The net amount on deposit at the bank is a consideration, however does not overrule any of the established policy procedures outlined herein.

NORMAL CLEARING PROCEDURES AND AVAILABILITY

The bank utilizes various modes of clearing checks, selecting that one mode which maximizes the overall availability of funds. The availability of funds varies depending upon the bank the item is drawn on which governs the mode of clearing utilized. This policy is based on the availability of funds on items deposited in the bank lobby and Drive-up facility prior to the ledger credit deadline of XX:XX (3:00 P.M.), as posted at the teller stations, on bank business days. The processing date of deposits received at the electronic banking devices is governed by the ledger deadline posted on the advice. Items may be released to clearing earlier in the day; however, this policy is based on the ledger credit deadline of XX:XX (5:00 P.M.) in order to allow for any normal delay in processing at the bank caused by system downtime, or degradation, volume, etc.

The modes of check clearings utilized at the bank are as follows. Listed for each clearing method are the items included in that method, as well as the established normal availability time based on float.

MODE	DEFINITION	AVAILABILITY TIME
Our bank's Processing Center	Items drawn on our banks demand or savings accounts, as well as items drawn on all banks processed by our processing center.	Current day
Local Clearing House	Items drawn on banks with an ABA number of xxxx (or banks also specify specific bank routing numbers if applicable such as xx-x xx-x).	Current day
Regional Clearings	Items with an ABA number of xxxx and xxxx plus all Government checks and U.S.. Postal Money orders.	1 Day
Federal Reserve Bank	All items that do not qualify for the above mentioned clearing modes or items received after the current days clearing deadline on any of the above mentioned modes.	Our non-P.O.D. bank has assigned a 1.5 day float on all items clearing througl Fed. This is based on the average float of all Fed. items.

MODE	DEFINITION	AVAILABILITY TIME
		Our bank will manually review the float on individual items if desired ar adjust the float accordingly. The maximum availability time applic shall not exceed or business day for ea bank involved in th clearing of the ite

Checks Drawn on Foreign Banks - Checks drawn on foreign banks are cleared by utilizing various modes. Our correspondent bank's International Depar ment selects the one mode which maximizes the overall availability of funds. Special consideration is given to Foreign Checks due to the clear ing modes between the U.S. and foreign country involved.

The correspondent bank's International Department, establishes and publishes the documented conversion schedule on a current basis. The fluctuation of the foreign exchange rates determines the frequency of an updated conversion schedule.

Our bank has the option to accept all foreign bank checks for collection only, or accept the checks for deposit with immediate funds availability subject to final payment.

Checks drawn on a foreign bank payable in foreign currency are converted to U.S. dollars at the time of deposit. The customer receives immediate funds availability because the conversion rate takes into consideration the established average float experienced by our correspondent bank at that time on the foreign country involved.

Checks drawn on a foreign bank payable in U.S. currency may be accepted for deposit at the bank. Our correspondent bank's International Department assesses the established documented fee based on the dollar amount of the foreign item which is passed on to our bank customer. These deposits receive immediate funds availability also as the fee takes into consideration the average established float experienced at our correspondent bank.

EXCEPTIONAL DELAYED FUNDS AVAILABILITY

The bank shall exercise its option to place an UNCOLLECTED FUNDS HOLD on an account if the bank has sufficient reason to deem it necessary to protect itself from risk of loss in the event deposited checks prove uncollectible. The bank shall not place an UNCOLLECTED FUNDS HOLD on an account for a longer period of time than the normal established clearing, return time frame. The bank shall conduct an annual 30 day study establishing the average clearing/return time frame for items processed by the bank. This documented study is used in determining the normal length of time experienced for returns. If an UNCOLLECTED FUNDS HOLD is placed on an item drawn on a specific bank that was not included in the annual study, the bank shall use a reasonable time frame based on an equivalent clearing area bank.

The UNCOLLECTED FUNDS HOLD may be placed on the account at the time of deposit, at the time of reprocessing the check, at the time the bank was notified by the drawee bank of the return of the check, or at the time the bank has sufficient reason to protect itself from risk of loss.

The bank may elect to exercise its option to forward a check for collect rather than accept it for deposit.

The bank has an option to delay the issuance of immediate credit on any Demand or Savings item deposited in order to allow for the processing of the item.

The bank can place an UNCOLLECTED FUNDS HOLD and return items accordingly on an account for any of the following reasons:

a. Kiting - The account has checks presented for payment prior to funds being collected and the bank suspects kiting of checks by

b. Any type of Court litigation such as Bankruptcy, Account Garnishments and Levies - The account may represent a potential loss to the bank when any of these conditions exist on an account; therefore, the bank has an option to place a hold on the account and pay against collected funds only.

c. Deceased Accounts - Due to the fact that any check deposited after death has an increased ratio of being returned because payment is not due the account holder after death, the bank may pay out on collected funds only.

d. Major Delay in Mode of Collection - If a major delay has been experienced in collecting the items due to weather conditions, strike, computer downtime, or any Act of God, the availability of funds can be adjusted accordingly.

e. Reprocessing of a Returned Item - If an item has been returned for NSF, incorrect ABA number, encoded/written amount discrepanc refer to maker, uncollected funds or any other reason and the customer has requested the bank to reprocess the item for cleari the bank may place an UNCOLLECTED FUNDS HOLD on the account unti sufficient time for the item to clear.

f. Fraudulent or unethical account holder activity - If the bank has just cause to believe that the account holder is practicing unethical business.

g. Unusual account holder activity - Based on the previous establis ed account history an unusual volume or dollar amount increase may indicate an exposure to loss for the bank, therefore an UNCOLLECTED FUNDS HOLD may be placed on the account.

LARGE ITEM RETURN PROCEDURE

It is suggested that all banks be required to implement the following procedures if the dollar amount of the item being returned is XX,XXX (25,000) or more or if the drawee bank has reason to believe the immediat return of the item is of utmost importance.

a. Notify the originating bank, by means of telephone or bank wire, immediately.

b. Return the item, along with a copy of the Fed debit/credit advice, directly to the original bank that presented the check for clearing.

c. Prepare a multiple copy Fed debit/credit advice that has been designed for this direct return procedure.

d. Forward the credit portion of the Fed advice to your bank's Fed Reserve Bank. Your Federal Reserve Bank is responsible for crediting your bank's account and debiting the appropriate Federal Reserve Bank where the originating bank maintains their account.

e. Automated means of transferring the credit/debit entries should be utilized if available.

EXHIBIT B

FUNDS AVAILABILITY

The practice of delaying funds availability is both a deterrent and a protective measure. It is a deterrent to the extent that fraud attempts are minimized. Would-be defrauders usually check a bank's delay practices. It is a protective measure to be used when, in the event a check is dishonored and returned, recourse is uncertain. The check system has the weakness of time lag for the physical return of dishonored checks to the bank of deposit. Unfortunately, there are those in our society who deliberately use the weakness to extract cash from financial institutions with no intention of restitution. Control mechanisms are necessary to contain losses at a reasonable level.

The terms Availability of Funds and Uncollected Funds are frequently interchanged, but have very different meanings. Provisional credit (availability) may be given by the Federal Reserve or a correspondent bank, but it is provisional subject to change back if checks are dishonored. The study of return items by three commercial banks in Denver, Boston and St. Paul indicates the time lag before items are returned (Exhibit A).

Check kiting is one of the most feared frauds perpetrated against banks. Some losses have been large enough to cause bank failure (Exhibit B). Kites can only happen if withdrawals are allowed on uncollected funds. Kiting is a concern of bank management, internal and external auditors and examiners (Exhibit C).

Law enforcement has not provided the kind of support to deter those who intentionally attempt to defraud or even help the unfortunate honest citizen caught in the middle. Whether it be lack of funding, difficulties with laws and prosecution or the inability to detect violators, the banks are left to their own devices for almost all of this activity. Delaying the availability of funds is the principal defense (Exhibit D).

Congress deemed it necessary to pass the Bank Protection Act in 1968 to establish minimum standards for security devices and procedures to control the bank robbery problem. The Board of Governors issued Regulation P to implement the Act. Although good statistics are not available, it is estimated that industry check losses far exceed losses from robberies. If it became mandatory to release funds in 2 or 3 days, the potential loss would be many times the current level. Such a rule would constitute an invitation for illegal check activity and would attract far more practitioners to our doors.

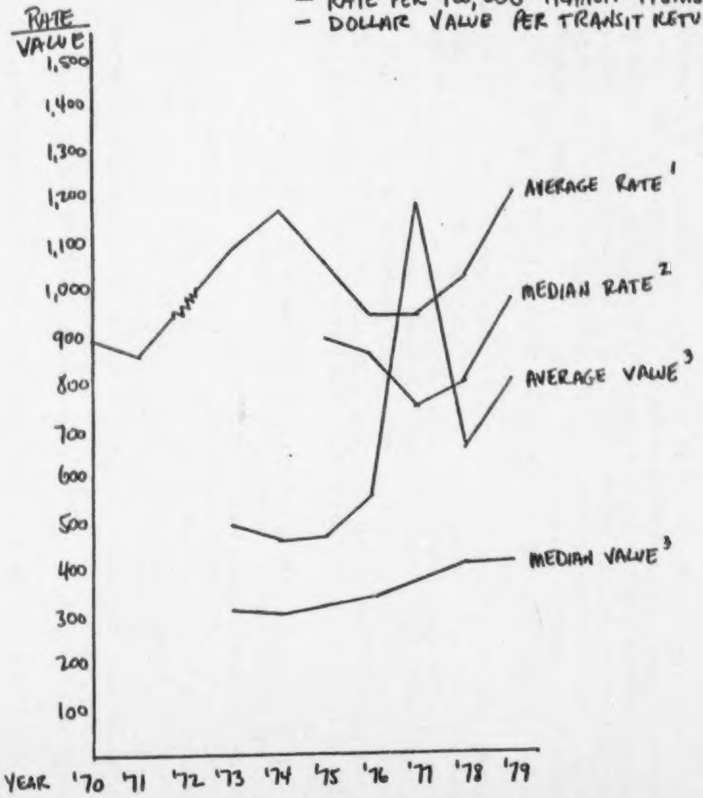
Within the industry, the approach to funds availability is varied. Some financial institutions use an "across the board" delay of usually 2–3 days. The majority exercise delays on an exception basis with the delay usually 5 days for local checks and 10 for out-of-town checks. Conditions vary by institution causing each to install the procedures best suited to their environment while minimizing customer dissatisfaction. It would be very impractical to expect all financial institutions to be able to operate with the same precautions and deterrents.

Because of all of the above it is suggested that the original recommendation submitted to the Board of Governors be reconsidered as the most practical and workable approach to funds availability. Essentially, the proposal contained the following:

1. A letter from the Board of Governors to each bank CEO suggesting a review of present procedures. Encourage other regulators to also send letters so that all financial institutions are covered.
2. Disclosure of funds availability policy.
3. Base practice on actual experience.
4. Promote an industry-wide program of communicating relocation services available at banks (Exhibit E).
5. Continue industry research on the reduction of return item time.

EXHIBIT A

TRANSIT RETURNS
- RATE PER 100,000 TRANSIT ITEMS SENT
- DOLLAR VALUE PER TRANSIT RETURN ITEM



DEFINITION: ITEMS RETURNED FOR ANY REASON THAT WERE ORIGINALLY SENT OUT AS TRANSIT ITEMS (ON-OTHERS).

1 1970 DATA FOR ADL BANKS ONLY. NO COMPARABLE DATA COLLECTED IN
2 COMPUTED ONLY SINCE 1975.
3 COMPUTED ONLY SINCE 1973.

DELAYED FUNDS AVAILABILITY

SUMMARY OF ONE WEEK SURVEY

		BANK A	BANK B	BANK C
1.	Checks Deposited/Cashed by Consumers			
	(a) Number	43,355	N/A	N/A
	(b) Dollar Value	$ N/A	$ N/A	$ N/A
2.	Checks Returned to Bank			
	(a) Number	3,922	9,238	6,724
	(b) Dollar Value	$789,851.58	$21,197,647.45	$7,991,968.27
3.	Consumer Drawn Checks Returned to Bank			
	(a) Number	2,949	N/A	N/A
	(b) Dollar Value	$744,622.50	$ N/A	$ N/A
4.	Items Charged Back to Consumer Accounts			
	(a) Number	33	171	39
	(b) Dollar Value	$ 14,342.13	$ 252,672.65	$ 10,443.90
5.	Time Range in Days From Date of Deposit to Date a Consumer Item is Returned to Bank			
	(a) 1-3 Days			Average 4.6 Days
	i) Number	923	56	
	ii) Dollar Value	$303,134.98	$ 109,219.65	
	(b) 4-6Days			
	i) Number	1,572	82	
	ii) Dollar Value	$353,954.36	$ 55,257.69	
	(c) 7-10 Days			
	i) Number	451	25	
	ii) Dollar Value	$ 86,719.70	$ 4,833.59	
	(d) More than 10 Days			
	i) Number	3	8	
	ii) Dollar Value	$ 813.46	$ 83,361.92	
6.	Outstanding After 3 Days			
	(a) Number	2026	115	
	(b) Percent	68.7%	67.3%	
	(c) Dollar Value	$441,487.52	$ 143,453.00	
	(d) Percent	59.3%	56.8%	

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The Prevention and Detection of "Kites"

The problem of payment against uncollected funds is a problem as old as banking. Payment of checks against uncollected funds, or float balances, is an extension of credit and this credit is extended on items over which the bank has no control; the items can be returned for any number of reasons. It is not the occasional user of float or uncollected funds that should be the concern of the bank's management. Generally that type of account is not the one that causes trouble. What management should be quite concerned about is the account that constantly uses uncollected funds. It should be apparent that a depositor who must draw constantly against uncollected funds is either under-capitalized, in trouble, or both. Therefore, any bank tolerating such a practice must expect trouble from such an account. When frequent withdrawals are allowed against uncollected funds, check-kiting may result. The use of uncollected funds does not necessarily mean a "kite," but a "kite" certainly means the use of uncollected funds.

"Kites" have caused losses large enough to entirely eliminate the total capital structure of a bank. Some banks would have closed as a result of a loss through a "kiting" operation except for the recovery effected under their bankers' blanket bond.

Generally, where employee dishonesty is not involved, bond-

EXHIBIT B

ing companies pay "kiting" losses under the "false pretense" coverage found in the "on premises" insuring clause of bankers' blanket bond, Standard Form No. 24. Some banks carry their bond coverage on the basis of a Form 24 as primary and a Form 2, a narrower and less costly coverage, as excess. It should be pointed out, however, that the Form 2 does not include "false pretense" as one of the perils insured against; a bank should weight carefully the idea of carrying all of its coverage, both primary and excess, on Form 24.

The term "kiting" may be defined as an operation whereby a depositor draws a check on "A" Bank for an amount in excess of the balance due him and then draws a second check on "B" Bank as a deposit to cover it, the second check, in turn, being covered by a third check drawn on "C" Bank; and the cycle being repeated over and over until these illegal operations are discovered. The elapsed time taken for these checks to clear through the respective banks may give the depositor sufficient time to adjust his various bank accounts before his scheme is detected. During the time his "kiting" of checks is in operation, he has had the use of bank funds without interest. During the cycle, one of the depositor's bank accounts in the respective bank shows an overdraft on his books. The time necessary for clearance between the respective banks must be carefully calculated to escape detection. The following example will illustrate the steps taken by the depositor in his manipulation of "kiting," as disclosed by his books of account with respect to the various bank accounts. It is assumed that he has legitimate deposits of $1,000 in each of three banks, one in his home town and two others in distant cities.

Failure to cover, in time, any one of the irregular "kite" checks deposited would lead to an overdraft in some one of the three banks and consequent exposure of this illegal operation. Some depositors have been forced to wire funds to cover the payment of "kited" checks in time. If it were not for the element of time required to clear checks this scheme would be difficult, if not impossible, to operate. In nearly every case, "kiting" begins by allowing a depositor to draw against uncollected funds. The "kite" begins with a relatively small amount and is gradually increased until it often results in bank-wreck-

EXHIBIT C

ERNST & WHINNEY MANAGEMENT LETTER

FEBRUARY 26, 1979

(9) DEMAND DEPOSITS

Uncollected Funds--The uncollected funds report currently available does not provide adequate information to detect check kiting. This report does not segregate the collected and uncollected funds balances, but instead lists the amount of the current day's debits which were paid from current day's deposits. In addition, no consideration is given to the source of the current day's deposits (i. e. cash, checks, checking plus, etc.).

There is another computer program which subjects each personal account to eight tests to check for possible kiting. The program is run twice each month and a list is produced of accounts meeting at least five of the eight tests. We were informed that the review of this report involves considerable time and effort since the report includes accounts which are not necessarily drawing on uncollected funds, but have heavy activity.

We recommend that a program be written to more effectively identify uncollected funds. The program could assign a fixed number of days required for a check to clear based upon the location of the payor bank. The program could then calculate the amount of the customer's balance which is uncollected and produce a report showing information on customers drawing on uncollected funds, similar to an overdraft report. Procedures could then be established to approve or reject the charges against uncollected funds.

Exhibit D

[From the St. Paul Dispatch, June 16, 1980]

Ball Bounces Wrong Way Trying to Collect Bad Checks

(By Les Layton)

Milo Ustipak is holding a $692 bum check that has convinced him people have a license to steal in St. Paul.

Ustipak, owner of West Seventh Street Auto Mart, 1419 W. Seventh St., did some major repair work on a four-wheel drive Dodge truck for a Crystal couple and accepted a $692.35 check.

The couple were polite and thankful for his efforts. Ustipak's bill was more than $300 below a Chrysler dealer's estimate.

But, the check bounced. Non-sufficient funds. Ustipak's bookkeeper sent it through a second time. It bounced again. He called the truck's owner. Phone disconnected.

Accompanied by an off-duty police officer, the businessman visited the Crystal couple. Nobody home. He contacted the fellow's employer. Laid off. He sent a notice of demand via certified mail. No response.

Finally, Ustipak notified his attorney and police. He got little satisfaction. But he was able to put a lien on the truck, clouding the title and preventing transfer of ownership.

Small claims court could render a judgment against the couple. There is no guarantee, however, he'll ever collect to satisfy the judgment.

The system, the auto repair man says, has let him down.

"The thing that bothers me most of all is that I'm here holding this $700 check and the city says, 'Hey, tough luck.'

"I'm sure if I walked into a restaurant and was charged with defrauding an innkeeper, I'd be in real trouble."

St. Paul Police Department officials informed Ustipak that because the truck's owner had made a deposit—even a $5 one—sometime prior to 30 days before he wrote the check, they don't have a chargeable offense. It is considered a bookkeeping error. That's assuming the Crystal couple are not writing numerous other bad checks.

Sgt. John Markuson, who worked on non-sufficient funds complaints for more than a year in the St. Paul city attorney's office, said the 30-day deposit rule makes it difficult to prosecute people who pass bad checks. Some are taking advantage of the guideline, he said, as bad checks increase during the recession.

"There were some people who were consistently writing bad checks and there was nothing we could do about it," Markuson said. "It's too bad."

Sgt. John Voita, Markuson's successor in the city attorney's office, agreed.

"I don't make the rules. Foley's office (Ramsey County Attorney Tom Foley) sets the policy and they don't take them (bad-check cases). It upsets me that someone comes in here and dumps some of these bad checks and ends up in Municipal Court when they should be charged with a felony."

Voita received several complaints Friday about non-sufficient funds checks for $1,000 or more and couldn't pursue any of them. Some were old; the police won't accept complaints on checks more than four months old. On another case, the check writer's bank would not provide the necessary imformation for investigators, citing the Data Practices Act.

Markuson said most law enforcement authorities "don't want anything to do with bad checks."

That's apparently the case, according to guidelines established by the city attorney's office and the St. Paul Police Department's fraud and forgery unit.

People can close an account and write checks on it for 20 days without being charged, according to the city attorney's criteria for obtaining a criminal complaint.

The police are even more lenient.

"The county attorney will not give us a complaint on an account-closed check unless the account was closed 30 days prior to the date the check was written," says a fraud and forgery unit memo given to officers investigating bad-check cases.

The same instructions say, if one of your employees accepted the check but you're not sure which one, "we cannot get a complaint." The same is true if you cannot identify the check writer.

The city attorney's guidelines indicate there are three other conditions which prevent prosecution. They are:

If the receiver said he would hold the check or allowed it to be post-dated;

If the check was in payment of a "past consideration;"

If the bank will not send information (monthly statements showing deposits and debits) needed on an non-sufficient funds check.

Authorities are turned off by merchants who want to use them as a collection agency, explained one law enforcement official, because business people are concerned if the person is charged or convicted only if they don't get their money.

The problem with convicting those who steal by writing bad checks is that the prosecution must prove the person's intent to defraud, according to Craig Forsman, assistant Ramsey County attorney.

"If he has an active account and has made some deposits in the recent past, it's almost impossible to prove beyond a reasonable doubt that at the time he wrote the check he intended to defraud or steal," Forsman said. "If the account was closed (at least 20 days earlier) and you can show that it was closed, that's another story. The other is if there were a number of (bounced checks)."

Forsman said that Ramsey County attorney's office is "hesitant to charge" a single bad-check case because it's almost impossible to convince a jury the check writer was intentionally defrauding someone. Citing one of the "world's greatest lies," Forsman said the person might have written a large check yesterday expecting another in the mail today to cover it.

He sympathized, however, with people like Milo Ustipak.

"It's a tough area because it's one of those situations where it's easy to see someone was wronged, but it is difficult for someone from a layman's point of view to understand why we didn't charge the case."

Forsman added that systems such as Tele-Check have made it difficult for people to pass large checks without sufficient funds.

In Ustipak's case, however, he accepted the check after the bank was closed. He was told by the dealer who sold the Crystal people the truck that the customers "were good" for the money.

And to make matters worse, Ustipak learned that when he opened the truck parts from White Bear Dodge to fix the truck, an item he paid for wasn't included. He had to purchase it elsewhere for $175.63. When he recently asked for the refund from White Bear Dodge, they were out of business.

Ustipak has had enough. Effective July 1, he will be involved in another business.

We can transfer your friends' banking services before they move to Arizona. And then, we'll even help arrange their furniture.

EXHIBIT E

Valley Bank's Quick Switch service.
One simple form makes it easy.

Why not help your friends move before they pack a single box?

Just call our Arizona Information Service.

We'll send them a Valley Bank Newcomer Packet containing our Quick Switch application that can transfer all their banking services ahead of time.

Plus they'll receive free maps and information about the area they're moving to.

Then, when their Quick Switch application is approved, they'll receive a card showing their personal account numbers. Their Arizona credit and identification will be available for them when they arrive.

Why choose Valley Bank?

We're the largest bank in the Rocky Mountain States. With over 190 offices throughout Arizona. And the most comprehensive range of banking services in the state.

Services like the Valley National Banking Card—the ultimate check guarantee card. Master Charge* and Visa,* with options like "Worry-Free Checking."* A variety of checking and savings accounts to choose from. And that's just the beginning.

One more way we'll help your friends.

As soon as we receive their Quick Switch application, we'll send them a free furniture-arranging kit. It makes it easier to figure out where everything will go—before they move.

Just call or write us.

Our number is (602) 792-7580. (You're welcome to call collect.) Or write: Arizona Information Service, Valley National Bank of Arizona, P.O. Box 311, Tucson, AZ 85702.

We go out of our way for you.
Arizona Information Service. Valley National Bank
Member FDIC

First National Bank has a warm welcome for your preferred customers moving to Arizona.

If you have a preferred customer moving to Arizona, we'd like to give him a warm welcome ...before he arrives.

All we need is an officer's letter of recommendation from you. Then we'll immediately issue your customer our exclusive VIP check cashing card for use until his accounts are established in Arizona. Upon presentation of the card at any of our more than 140 offices throughout the state, your customer's personal checks on your bank will be honored up to $500. No other identification will be required.

In addition, we'll send him our famous Newcomers Information Kit. It's packed with booklets, maps, and tips for new residents and contains a signature card which can be filled out and mailed to us. We'll handle all the paperwork for an easy transfer of funds for your customer so his banking relationship will be well established before his move to Arizona.

When the checking account is opened, your customer will be issued a check guarantee card. The Western Bancard which unequivocally guarantees personalized First National Bank of Arizona checks for up to $600 in merchandise or services or $100 in cash at any of our more than 17,000 merchants statewide.

Western Bancard will also guarantee that your customers personalized First checks will be honored at more than 800 offices and the 22 Western Bancorporation affiliated banks in 11 Western states.

For further information and a supply of brochures describing our preferred customer service, call or write:

G. Reed Macomber, Vice President
First National Bank of Arizona
P.O. Box 20551
Phoenix, Arizona 85036
(602) 271-1471

The First
FIRST NATIONAL BANK OF ARIZONA

More than a name, it's a promise.

You can get your customers off to a good start in Arizona.

You've given your customers the kind of service they deserve. And now that they're moving to Arizona, you can do them one more service to make the move easier. Talk to them about Valley National Bank.

We're the largest bank in Arizona with over 180 offices statewide. So anywhere your customers are moving to in Arizona, a Valley National Bank will be there. With every banking service they will ever need. And more.

Everything they want to know about Arizona.

Our Arizona Information Portfolio is specifically designed for the newcomer. It combines both state and community literature with highlights on housing, taxes, schools and recreation.

Our "Quick Switch" service makes their switch quicker.

"Quick Switch" is an exclusive service of Valley National Bank. It's a simple method for establishing a total banking relationship before the move. So your customers can have their personal accounts open and waiting when they arrive.

Our Hotline makes the welcome warmer.

We accept collect calls on our Hotline (602) 261-1500 so that we may answer any questions, supply information and give assistance in any way we can.

We hope we'll be hearing from you. And your customers. Call (602) 261-1500.

VISA
ARIZONA

We go out of our way for you.
Valley National Bank

MEMBER FDIC

INTRODUCTION

This Brochure is provided for your information. We feel that it is important that you understand the specific services we provide when you open an account and the rules and conditions under which we must handle your account.

The general rules and conditions which apply to all depository customers are presented first. It is important that you understand these rules. Next, the specific rules and agreements pertaining to certain banking services (for instance checking) are covered in the individual service sections. Also included is a Schedule of Fees which covers the various regular and special charges associated with our services.

Please take a few minutes to review this booklet and then keep it with your other banking papers. If you have questions which are not covered here, please contact your Personal Banker. Your Personal Banker is:

First Bank Saint Paul
Member First Bank System

Main Office: 332 Minnesota St. 291-5231
Battle Creek Office: 1959 Burns Ave. 738-9662
Shoreview Office: 1001 West Highway 96 482-1200

A Full Service Bank
Member FDIC

GENERAL RULES AND CONDITIONS

Agreement

When you apply for an account with us, you are asked to complete an application indicating the accounts or services you desire. If an account is opened, your signature on that application represents your acceptance of the terms and conditions pertaining to your account.

Authorized Signer

When you opened your account, you specified who would have signature authority over your account. If you are a new customer, a signature card was prepared for your signature. If you already have a relationship with our bank, your signature is on file. We will not honor any withdrawal orders or checks unless the signature matches that of an authorized signer. If more than one authorized signer was designated, then any one of the signatures would enable us to honor the withdrawal unless other arrangements had been made at the time the account was opened.

Deposits

All deposits which are made in some form other than cash are subject to final payment. If we are unable to collect the item, we have the right to charge the item back against your account. All deposit receipts are subject to later count and verification of the items deposited; any errors will be corrected by us and you will be notified. In addition, any deposit made by drop box is made at your own risk as to verification of the amount.

Availability Of Funds

Our policy is to provide the earliest availability of funds on deposited checks as is realistic. However, we reserve the right to place withdrawal restrictions on these funds for a period sufficient to receive notification that a check has been dishonored. Any delay of availability will not exceed the normal time required for a notice of dishonor.

Restrictions or holds on withdrawals of funds shall be limited to a maximum of 10 working days. Restrictions may be placed on cash back or split deposits and deposits to new accounts providing that we inform you of the restriction the reason for it and the time duration. Checks deposited to established accounts (90 days old) will normally be accepted without restriction.

If you have questions regarding this policy, see your Personal Banker.

Joint Accounts

These accounts are ones which may be used by more than one person as if it was each person's own account. Each person, called a "joint owner", may deposit or withdraw funds from the account and may at any time withdraw, close or transfer the account without the consent of other owners of the account. If one joint owner dies, the account becomes the property of the surviving joint owner. If there are two or more surviving joint owners, their interest remains that of joint owners of the account.

Deposits By Mail

If you mail deposits to us, we cannot accept responsibility for them until they are received at the bank. If you mail a cash deposit, you do so at your own risk. If you must send cash, do so by Registered Mail.

Automatic Transfers

You may instruct us to make transfers from an account on a regular or periodic basis. Due to Federal Regulations, pre-authorized transfers and/or telephone transfers from Statement Savings accounts are limited to a total of three per calendar month. Depending upon the type of transfer, there may be a service charge. Special instructions are required for these transfers and the arrangements may be made with your Personal Banker.

Telephone Transfers

If you have both a Statement Savings and a checking account at our bank which have identical titles, you may transfer funds between them by simply calling our Telephone Transfer. Due to Federal Regulations, pre-authorized transfers and/or telephone transfers from Statement Savings accounts are limited to a total of three per calendar month. The minimum amount for each transfer is $50.00. The rules which apply to Telephone Transfers are covered in the "Important Customer Information About Electronic Banking Transactions" pamphlet provided by your Personal Banker. Because these transfers are accomplished over the phone, they are not immediately processed. It may take us up to one business day to perform the bookkeeping, verify the authenticity of the transaction and make the transfer.

Right to Set Off

If we have extended credit to you or your joint depositor, or if either of you owe us money on an obligation which is not being promptly repaid, we may charge any such joint account for all or any part of the debt. This rule will also apply should you die before repayment.

Service Charges

We may assess against your account reasonable charges based upon account balance, activity, inactivity, returned items, overdrafts, stop payment orders or other special services. The service charges are explained in the "Schedule of Fees" section. Other service charges can be explained by a Personal Banker.

Garnishments or Attachments

If we are served with a legal process which seeks to attach or in some manner restricts you from freely using your funds, we reserve the right to hold any part of the funds until it is finally determined who has a legal right to the funds. At that time, we will pay any balance in the account to the proper party. We reserve the right to charge a fee for this procedure.

Power Of Attorney

This is a special relationship by which someone is given the authority to make account transactions for the benefit of the owner of the account. There are forms available at the bank for establishing this relationship.

Automatic Teller Machines/FirstBank Cards

There are various types of Automatic Teller Machines which may be used by you in performing banking business. All of these Automatic Tellers, both on and off our bank premises, must be activated with a FirstBank Card which can be obtained from the bank. The laws pertaining to the use of Automatic Tellers and your rights and responsibilities with regard to them are very specific. A separate pamphlet on Electronic Banking Transactions which was provided by your Personal Banker, discloses these rules, rights and responsibilities. It is important that you review this pamphlet before first using your card.

Disclosure of Information

Your account is confidential information which we do not divulge except to bank examining authorities or in response to a court order or validly issued subpoena or if you have given the banks name as a credit reference on a credit application to the party to whom you are applying for credit. We will notify you in writing if account information is released in response to a court order or validly issued subpoena.

Closing Your Account

You may close your account at any time upon written notice to us. We reserve the right to close your account upon due notice, and remit the balance to you by Cashier's Check.

Abandoned Accounts

If we have no record of any deposits, withdrawals or communications from you on your account for seven years, state law requires us to report this fact to the state. Thereafter we will be required to deliver the account balance to the state as abandoned property subject to your claim if we cannot locate you. If your account becomes dormant, we will try to locate you at the last address and telephone number you provided us. If you change address, please notify us so your property kept with us does not become abandoned. We reserve the right to impose a reasonable fee (See Fee Schedule) for processing abandoned property.

Amendments To Rules And Conditions

These rules and conditions may be changed by us by posting the changes in the bank lobby at least 30 days prior to the effective date of the change. In addition, if changes in federal or state banking laws cause conflicts with the rules outlined in this book, those government regulations will prevail.

CHECKING PACKAGES

We now offer two checking plans, with variable payment methods and additional available services. Each plan is subject to special fees, rules, and conditions. You should carefully review any information which pertains to your account.

Savers Checking

Savers Checking is tied to a customers Regular Savings or Savings Certificate balance. With Savers Checking you get free checking and the Red Carpet package of services (see page 11) at no charge.

By maintaining a $3,000 Regular Savings, or a $10,000 Savings Certificate balance, you receive all the benefits of Savers Checking plus you earn interest on the money you keep in your checking account.

When you maintain a $2,000 Regular Savings balance, or a $5,000 balance in qualifying Savings Certificates, you receive free checking and the Red Carpet Package at no charge.

- If you fail to maintain the minimum balance in the separate savings or certificate account for the Savers Checking you select, we are authorized to charge you a service charge. See Schedule of Fees for the exact amount.
- The monthly service charge is waived so long as the minimum savings/certificate balance is maintained.

Basic Checking

Basic Checking, as the name implies, is for the customer who desires only a checking account. There are three methods of payment for Basic Checking:

- Minimum Balance*
- Monthly Flat Fee
- Per Item

*There are two Minimum Balance options. First, if you maintain a $300 minimum balance you receive free Basic Checking. Second, if you maintain a $1,000 minimum balance, you may elect to earn interest on all of your funds by choosing the Interest/Checking option.

- If you fail to maintain the minimum balance requirement we are authorized to charge you a service charge. See the Schedule of Fees for the exact amount of the charge.

The Red Carpet package is available with any of the Basic Checking plans for a monthly fee. See the Schedule of Fees for the exact amount.

Note: With the Interest/Checking option under Savers Checking or Basic Checking, we reserve the right to require 14 days notice from you for any withdrawals.

Red Carpet Package

The Red Carpet package is designed for the customer who needs a variety of banking services. The package is provided free with Savers Checking and for a monthly fee with Basic Checking (see the Schedule of Fees for the exact amount). As a Red Carpet package customer you are a member of the Personal Financial Services Association which allows you to obtain the following services:

- Special personalized checks free of charge.
- Free Bank of America Travelers Cheques.
- $5,000 Personal Accident Insurance.
- A Safe Deposit Certificate which entitles you to:
  - A free standard sized Safe Deposit Box, or;
  - $10.00 credit toward a larger box.

Note: This privilege will remain in effect as long as you are a Red Carpet package customer. If your Red Carpet package is terminated, any subsequent Safe Deposit rental fees will be your responsibility.

The monthly Red Carpet package fee will be assessed against your checking account automatically. If the assessment of the monthly fee causes an overdraft your account will be service charged for the overdraft. See the Schedule of Fees for the amount of this charge.

THESE RULES APPLY TO ALL CHECKING ACCOUNTS:

Statements

We will periodically mail, or in some other manner make available to you, a statement of your checking account with cancelled checks and/or other documentation which reflect the transactions that have occurred during the period covered by the statement. You should examine them promptly and report any differences to us within 16 days of the date the statement was mailed. If you do not, we cannot be responsible for any erroneous payments.

Post Dated Checks

We will honor in good faith, any check which shows an authorized signature. But, as a practice, you should not post date a check unless you are certain the payee will hold it until the date of the check.

Stop Payments

You may advise us to stop payment on any check you have issued against your checking account. The authorization for a stop payment is valid for 14 days. If confirmed in writing within that period, it is effective for 6 months, and longer if renewed. You should realize that there are times when your stop order will not prevent payment from being legally enforceable against you. Here are some simple rules concerning stop payments:

1. The order must be given to us in time for us to take action before the check is presented for payment. One normal working day is usually enough time for us to make the proper bookkeeping entries.
2. If the person you wrote the check to cashes it, and the new holder does not know of your order, the new holder may be entitled to collect the amount from you even though we didn't pay it when the check was presented to us.

3. The information you give us must be accurate as to: amount, check number and payee.
4. If the bank pays an item even though it has received a timely stop payment order, the bank may charge the depositor's account in the amount of the item. The charge will stand unless and until the depositor proves the fact and amount of loss resulting from payment of the item contrary to the stop payment order and that in paying the item the bank failed to exercise due care.

See the Schedule of Fees for the stop payment charge.

SPECIAL INVESTMENTS

First Rate Fund

First Rate Fund is a Retail Repurchase Agreement offering the advantages of a money market fund plus the solid backing of First Bank Saint Paul assets and a U.S. Government Security. A First Rate Fund requires a minimum investment of $3,000. The minimum reduction from your investment is $500. If your investment falls below $3,000, you will be assessed a service charge of $35. Investments under this program are not deposits, are not insured by the Federal Deposit Insurance Corporation (FDIC), and are not guaranteed in any way by the United States government or any agency thereof. Details on the First Rate Fund are outlined in the current Offering Brochure and Repurchase Agreement available at each office of the bank.

SAVINGS

The bank has several savings plans from which you may choose according to your savings goals. Each of these plans have different features, and again, special rules and conditions.

Statement Savings

- Statement Savings Accounts pay a base rate of 5¼% interest per year. Interest is compounded daily and posted quarterly for an effective annual yield of 5.39%. Earned interest is credited the first day following the end of each calendar quarter. All Personal Statement Savings Accounts are not transferable except on the books of the bank.
- If you have a Statement Savings Account, your account transactions will be reflected in a periodic statement which we will mail or in some other acceptable manner make available to you. This account must be reconciled in much the same manner as your Checking Account. No passbook is issued. We reserve the right to require 14 days notice from you for any withdrawals.

Passbook Savings

- Passbook accounts also pay 5¼% interest per year. Interest is computed daily and posted and compounded quarterly for an effective annual yield of 5.35%. Earned interest is credited the first day following the end of each calendar quarter.
- We don't always, but may at any time, require that you present your passbook for recording of account transactions. If you make transactions without presenting your book, you should have the book updated periodically. Mail transactions will not be reflected in your book unless you bring (or mail) it to us for updating. We reserve the right to require 30 days notice from you for any withdrawals.
- If you lose your book, we will replace it; however, there are precautions we must take and this might involve your posting a bond.

Savings Certificates, Investor Certificates

If you open one of these accounts, you receive a Certificate rather than a Passbook or Statement. Savings Certificates have a set maturity date and all are automatically renewable. Investor Certificates are also automatically renewable, unless a fixed maturity is requested. Tax Relief Investor Certificates require a fixed maturity of one year and lose tax benefits if any portion is withdrawn before maturity. With all Certificates, government regulations require a substantial interest penalty for early withdrawal.

Individual Retirement Accounts, Keogh Plans

The rules and regulations governing these accounts are very specific. When you open either of these accounts, these rules and regulations are disclosed to you. It is important that you review this information.

THESE RULES APPLY TO ALL SAVINGS ACCOUNTS:

Transferability

All savings deposits are transferable only on the records of the bank.

Payment Of Interest On Savings Plans

The amount of interest we can pay on deposits is determined by various federal regulations. The size, duration and withdrawal privileges with respect to each deposit affect the rate of interest payable. We set our rates in order to be competitive, our rates are publicized through advertising and by posting them in our bank. Once established, our rates will not change for at least 30 days after the change has been posted in the bank or otherwise made public.

Senator CHAFEE. The surveys we've conducted show that the delays are quite long in some instances—21 business days, Mr. Messina, in some instances in the S. & L.'s. In the banks you represent, Mr. Arner, would you say that you don't have a uniform delay payment situation but it depends upon the familiarity with the customer, the customer's record as outlined by Ms. Del Bucchia earlier?

Mr. MESSINA. Clearly, it depends on many, many factors. I might add, I don't argue with the fact that your survey revealed an institution with a 21-day hold condition. The league's recent survey conducted with 67 savings and loan associations covered check hold time frames from 1 to 21 days. Of the 67, none had holds beyond 15 days. Whether or not that 67 is a reasonable sample of the norm or whether or not it's truly extreme, I'll assume it does reflect a reasonable average. But, again, I don't question the fact that some institutions indeed might have very unreasonable hold policies in place.

Senator CHAFEE. What are both your associations doing about this whole subject, if anything?

Mr. MESSINA. In the State of New York—I might add that the New York State Banking Department does require truth-in-savings disclosures and, as such, we do provide complete disclosures including those dealing with check clearance and availability times.

I might offer, however, that oftentimes, no matter how fully we attempt to disclose, there still remains a fair number of consumers who obviously don't read, don't understand, or don't perhaps concern themselves with an issue until, in fact, it's right there and faces them absolutely.

Senator CHAFEE. Do you have a copy of those New York State—it's not a regulation, is it?

Mr. MESSINA. If I'm not mistaken, I believe the New York State Banking Department requires that banks falling within its jurisdiction provide what is commonly termed as disclosure statements.

Senator CHAFEE. Could you send me a copy of that statement?

Mr. MESSINA. I'd be delighted.

[Copy of disclosure statement follows:]

NOW account disclosure statement

NOW ACCOUNTS

Your NOW account at Columbia Savings earns the highest annual rate allowed by federal regulation, currently 5.25%. However, interest will only be earned at the end of each business day in which your account balance is $1,000 or more.

ANNUAL PERCENTAGE YIELD: If you leave your money on deposit for a full 365-day year and leave the earnings in your NOW account, you will earn interest at an annual percentage yield of 5.47% (5.48% in leap year).

For example, if you deposit $1,000 on January 1 and don't withdraw any of the deposit or earnings until December 31, you will earn $54.70.

HOW INTEREST IS EARNED ON YOUR ACCOUNT:

a. The Compounding Period: We compound interest each day.

b. You will earn interest each day your account balance is $1,000 or more by applying the Daily Percentage Rate of .000145833 to the balance in your account at the end of the day.

For example, you will earn 14.58 cents per $1,000 on deposit each day. The amount of interest you earn for one day will be added to the principal. You can find out the next day's interest by applying the daily percentage rate to this new principal.

c. The Association incorporates your daily interest for Friday, Saturday and Sunday as described below:

I.	Friday Balance	$1,000.00
	Daily Percentage Rate	X .000145833
	Interest for Friday	.145833
II.	Friday Balance plus interest	$1000.145833
	Daily Percentage Rate	X.000145833
	Interest for Saturday	.145854
III.	Friday Balance plus interest for Friday and Saturday	$1000.291687
	Daily Percentage Rate	X.000145833
	Interest for Sunday	.145876

Your actual daily interest rate for Friday is the sum of the three interest calculations (Friday, Saturday, Sunday). For example:

Calculated Interest for Friday	.145833
Calculated Interest for Saturday	.145854
Calculated Interest for Sunday	.145876
Total Interest Earned for Friday	.437563

WHEN YOUR DEPOSIT BEGINS TO EARN INTEREST: Your deposit begins to earn interest immediately, except:

a. If you make a deposit any time on Saturday or Sunday, your deposit will begin to earn interest on the following **Monday.**

YOU MUST MAINTAIN A MINIMUM BALANCE IN ORDER TO EARN INTEREST:

a. To earn interest on any day your account must have a balance of at least $1,000 at the end of the day.

b. If you withdraw all your funds before the end of the quarter, you will lose all the interest you have earned during the quarter. To receive your quarterly dividends, a minimum balance of $1.00 must be in your account on dividend posting day.

YOU MAY HAVE TO PAY US A SERVICE CHARGE: We may charge you the following fees:

a. $3.00 for each stop payment authorization.

b. $3.00 for each of your checks which the Association must return because of insufficient or uncollected funds.

c. $3.00 for each of your checks which you request the Association to certify.

d. $2.00 for a check or any other instrument deposited in your account and returned to us unpaid.

e. $3.00 for each duplicate copy of a paid check or a monthly statement.

Any such charges may be deducted from your account and the Association shall not be liable for dishonoring items because of insufficient funds resulting from such charges.

f. Pro rata share of costs related to or incurred by the association for remitting the funds to the State where accounts are deemed to be abandoned.

WHEN WE WILL PAY YOU THE INTEREST YOU HAVE EARNED ON YOUR ACCOUNT:

a. You earn interest on your account each day. (see previous section on "How Interest is Earned On Your Account") These earnings are posted on your monthly statement at the end of each quarter.

b. Although your account earns interest each day you may not withdraw these earnings until the end of the quarter when these earnings are posted to your monthly statement.

WHEN YOU MAKE A WITHDRAWAL AGAINST A CHECK WHICH YOU HAVE DEPOSITED INTO YOUR ACCOUNT:

The following is our schedule for determining when you may make a withdrawal against a check which you have deposited into your **established** NOW account. Availability days do not include the day of deposit.

	Availability
a. Cash	immediately
b. Checks on our bank	immediately
c. Checks (whether or not certified) on local banks, postal money orders	5 **business** days
d. Checks drawn on all other U.S. banks	10 **business** days

UNDER CERTAIN CIRCUMSTANCES, WE MAY REFUSE YOUR WITHDRAWAL REQUEST:

Under certain circumstances, we can refuse to permit withdrawals from your account. For example, we can refuse to permit a withdrawal from your account if:

a. We decide to require up to 60 days advance written notice of any intended withdrawal from your NOW account with us and we have not received that notice. If this happens, we must notify the Superintendent of Banks that we are exercising this option.

b. The withdrawal would consist of money deposited in the form of a check or money order and not yet available for withdrawal.

c. The person(s) with whom you have a joint account tells us not to permit a withdrawal.

d. A court orders us not to permit the withdrawal.

e. The account is pledged as collateral for a debt.

f. The withdrawal would consist of funds we have transferred out of the account to pay an overdue debt to us.

g. Any document or identification we require or the law requires in connection with the withdrawal has not been presented to us.

WHAT HAPPENS IF YOUR ACCOUNT BECOMES INACTIVE:

a. Your account will be considered inactive only if **all** of the following happens for one full year:

- i. No deposit is made into your account; and
- ii. No withdrawal is made from your account; and
- iii. We do not receive any correspondence from you which indicates that you know your account with us is still in existence.

b. If your account remains inactive for **four additional years,** it will be turned over to the State of New York. However, you may reclaim this money from the Bureau of Abandoned Property; New York State Department of Audit and Control; Albany, N.Y. 12236

WE WILL TELL YOU ABOUT ANY CHANGES IN THIS INFORMATION:

a. We may change the terms of your account, but if the change is unfavorable to you, we will give you written notice.

b. If the change is favorable to you, we will post the change in all offices of the bank and we may, also, give you written notice.

WHERE YOU CAN GET FURTHER INFORMATION:

Our branch manager will help answer any questions you may have about your account.

A daily interest factor table is available for review by depositors at all association offices.

Senator CHAFEE. Senator Dodd.

Senator DODD. That survey of 15 days, that's 3 weeks. I don't want to press, but don't you find that—what are you using? The Pony Express?

Mr. MESSINA. Those are extremes, Senator, if I may. They are, first, reflected in calendar days, and the greatest majority—and I will take as a sample metropolitan area serving less than 1 million people—the majority of associations seemed to apply a 1- to 3-day hold; 28 in fact; 34 percent apply a 4- to 5-day hold; 22 percent apply a——

Senator CHAFEE. But those are in-State or in-city, those holds?

Mr. MESSINA. That's generally speaking. Within the State I've got other numbers. Those are local checks.

Senator DODD. Those are all local?

Mr. MESSINA. All local checks.

Senator DODD. Run those figures—give me from three to seven—what's one to three?

Mr. MESSINA. One to three days is 28 percent. Four to five days is 34 percent; six to seven days, 22 percent.

Senator DODD. What are you using? Don't you find that to be outrageously long?

Mr. MESSINA. Not at all.

Senator DODD. In an in-State operation?

Mr. MESSINA. I might offer again, although it isn't absolute in its final sense, that recent 3-week survey and that recent 3-week experience that my institution had, suggests that 5, 6, or 7 days is clearly, in my view, a reasonable hold period. I might also add, as I suggested before, that the majority of savings and loans don't retain earnings or credit. What they do is simply attempt to minimize their risk of loss. As well, the majority of S. & L.'s who place holds are extremely lenient in waiving those holds for established customers and so on and so forth. And last, the majority of S. & L.'s only appear to place holds on about one-third of the total checks they receive.

[Copy of survey referred to follows:]

SURVEY OF SAVINGS AND LOAN ASSOCIATIONS
REGARDING DEPOSIT HOLD POLICY
FEBRUARY 1982

STATISTICAL TABLES

Table 1

CLASSIFICATION OF SURVEY RESPONDENTS BY SIZE AND TYPE OF MARKET AREA

	Number of Respondents By Size Within Type of Market Area			
Assets ($Millions)	Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban	Total
$0 - 49	-	-	-	-
$50 - 249	2	9	13	24
$250 - 999	4	18	2	24
$1,000+	14	5	-	19
Total	20	32	15	67
Average Assets ($Millions)	$1,060	$480	$180	$590

Table 2

DISTRIBUTION OF ASSOCIATIONS BY LENGTH OF DEPOSIT HOLDS

	Distribution of Respondents by Type of Market Area		
Length of Hold (Calendar Days)*	Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
Local Check			
None	10%	3%	13%
1 - 3	20	28	13
4 - 5	40	34	34
6 - 7	25	22	33
8 - 10	5	13	-
11 - 15	-	-	7
16 - 20	-	-	-
21+	-	-	-
Total	100%	100%	100%
Median	4 days	4 days	4 days
Within State, Nonlocal			
None	10%	-	13%
1 - 3	-	9%	-
4 - 5	20	22	13
6 - 7	35	22	34
8 - 10	15	25	13
11 - 15	15	19	27
16 - 20	5	3	-
21+	-	-	-
Total	100%	100%	100%
Median	7 days	7 days	6 days
Out-of-State			
None	10%	-	13%
1 - 3	-	3%	-
4 - 5	15	9	-
6 - 7	15	9	7
8 - 10	20	25	13
11 - 15	35	32	60
16 - 20	5	3	7
21+	-	19	-
Total	100%	100%	100%
Median	9 days	11 days	11 days
Number of respondents	20	32	15

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*Holds stated in business days have been converted to equivalent calendar days.

Table 3

PERCENTAGE OF RESPONDENTS ALLOWING VARIOUS EXCEPTIONS TO DEPOSIT HOLDS

Condition Under Which Hold Is Waived	Percentage of Respondents Waiving Deposit Holds for Specified Conditions by Type of Market Area: Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
Type of check deposited:			
Government check	83%	88%	92%
Payroll check	72%	91%	77%
Cashier's check	61%	81%	85%
Type of customer making deposit	61%	81%	62%
Number of respondents*	18	32	13

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*Excludes those that do not apply holds.

Table 4

PERCENTAGE OF DEPOSITS HELD

Percentage of Deposits Held	Percentage of Respondents by Percentage of Deposits Held Within Type of Market Area: Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
0%	11%	-	13%
1 - 20%	28	48%	34
21 - 40%	17	19	-
41 - 60%	11	7	20
61 - 80%	5	15	33
81 - 100%	28	11	-
Total	100%	100%	100%
Median percentage held	33%	22%	43%
Number of respondents	18	27	15

Table 5

POLICY ON NOTIFYING CUSTOMERS ABOUT DEPOSIT HOLDS

Type of Customer Notification	Percentage of Respondents Using Various Methods to Notify Customers of Deposit Holds by Type of Market Area Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
Teller informs customer when hold is placed on deposit	55%	72%	62%
Rules of account furnished customer describe hold policy	65%	66%	62%
Deposit ticket describes hold policy	15%	3%	23%
Leaflet provided at teller window or in lobby describes hold policy	30%	22%	8%
Customer can determine available balance by inquiry at ATM	5%	9%	8%

Table 6

POLICY ON RETURNING CHECKS REPORTED AS DRAWING ON HELD FUNDS

Return Item Policy	Percentage of Respondents by Return Item Policy Within Type of Market Area Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
Return automatically	6%	7%	9%
Review item before return	94	93	91
Total	100%	100%	100%
Number of respondents	16	29	12

Table 7

DISTRIBUTION OF ASSOCIATIONS BY FREQUENCY OF ITEMS RETURNED FOR DRAWING ON HELD FUNDS

Number of Checks Returned for Drawing on Held Funds Per 100,000 Checks Processed	Distribution of Respondents by Type of Market Area		
	Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
None	23%	23%	50%
1 - 10	31	26	8
11 - 25	8	23	14
26 - 100	23	19	14
101 - 200	15	9	7
201+	-	-	7
Total	100%	100%	100%
Number of checks returned per 100,000 checks at median association	9	11	1
Average (mean) number returned per 100,000 checks	66	26	27
Number of respondents	13	31	14

Table 8

DISTRIBUTION OF ASSOCIATIONS BY LOSSES PER ACCOUNT PER YEAR INCURRED FOR PAYING CHECKS DRAWING ON HELD FUNDS

Average Loss per Account per Year	Number of Respondents by Loss per Account per Year Within Type of Market Area		
	Large Metropolitan 1,000,000+	Metropolitan 100,000 to 1,000,000	Small Town and Suburban
0	5	15	13
$0.01 - 0.25	4	6	2
$0.26 - 1.00	6	4	-
$1.01 - 2.50	2	1	-
$2.51+	-	3	-
Number of respondents	17	29	15
Average loss per account	$0.71	$0.67	$0.02

Table 9

RETURN ITEM EXPERIENCE
OF COLUMBIA SAVINGS AND LOAN ASSOCIATION
NEW YORK, N.Y.

FEBRUARY 11 - MARCH 1, 1982

Number of Days Required to Receive Return Item*	Percentage of Items	
	Local	Nonlocal
Less than 7	-	-
7 - 9	9%	5%
10 - 12	37	5
13 - 15	44	29
16 - 18	5	45
19 - 21	1	11
22 - 24	1	5
25 - 34	1	-
35+	2	-
	100%	100%
Number of items	213	38

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*From date the check was deposited with S&L's bank to date it was returned to S&L.

Senator Dodd. Is it a policy of the institutions to, of course, invest those funds during the float period?

Mr. Messina. I would assume so.

Senator Chafee. Excuse me. Unfortunately, I have a longstanding prior commitment that I'm late for. Senator Dodd, if you would be good enough just to conclude here, I have to leave, but I thank you gentlemen for coming.

I would like to say it's the purpose of these hearings not in any way to increase the risks of loss. That's not what we're attempting to do. What we are attempting to do is to insure that the consumers are informed. That seems to me is where the greatest problem arises.

And, second, that the institutions conform their practices to actual experience and not have unreasonable delays—21 days, that's it, arbitrarily, for example, even though the time is way shorter. And what we want to do is expedite the return process, the notification electronically or whatever it might be, in order to reduce the risk of loss.

So I want to thank each witness who came and, unfortunately, I have to depart, but I thank you for taking over, Senator Dodd.

Senator Dodd. Not at all, Mr. Chairman. I was just going to markup a couple of bills while you're gone. Don't worry about it. [Laughter.]

Senator Dodd. Let me, if I can, just run down some things here. You're familiar, obviously, with that 1979 study because the ABA worked in conjunction with the Fed. First of all, the report recommended that the Board of Governors recommend that each bank have a written policy of delay-funds availability consistent with the task force recommendations. What action has the Fed taken since 1979 regarding that?

Mr. Arner. That recommendation was never implemented.

Senator Dodd. Let me ask you, the report recommended that the policies of the banks be defensible on a basis of its check-collection records and not exceed the normally expected return clearing period.

The survey we have done, and apparently based on ones Mr. Messina has done, as well, on the S. & L.'s, shows a wide variation with little or no apparent connection to the banks' actual experience.

Do you see something different than I do?

Mr. Arner. First of all, the variation is real. Check collection from St. Paul, Minn. is a different—it may end up with results different from those in New York, for instance, and I suspect that those financial institutions that have automated to a fairly high level are constantly analyzing their collection system to determine the best possibility in terms of availability.

So it may take, obviously, 1 day for collection of a Wisconsin check from where I am, but from there it might vary. I'm not sure that all institutions have analyzed completely their experience on return items, which is the basis of what we're talking about—the return-item experience.

Senator Dodd. Now, in connection with that, the report recommended that the Fed write to each CEO of each bank a letter on its position, on recommendations one and two as I mentioned. Was that done?

Mr. **Arner**. To my knowledge, that was not done, and our recommendation was based simply on the notion that maybe that would add some clout.

Senator **Dodd**. But it wasn't done?

Mr. **Arner**. Correct.

Senator **Dodd**. The report recommended further that the Fed consider requiring each bank to have a written policy and disclose the policy. Well, obviously, we know that hasn't been done either.

Fifth, the recommendation was that the Fed communicate the work of the task force to other Federal financial institutions regulators. Was that done?

Mr. **Arner**. I can't respond to that. The intent was that we were a commercial banking task force and we felt some of the complaints we were looking at were from other types of financial institutions and therefore——

Senator **Dodd**. But to your knowledge, it was not done?

Mr. **Arner**. Not to my knowledge.

Senator **Dodd**. I wonder if you might find out the answer for us on that. The report recommended that the ABA initiate the necessary action to accelerate the return of dishonored items. I gather some action has been taken in this regard, although it's going into the third year. What has happened to the charge to the ABA to develop a new financial service to meet the needs of a new customer?

Mr. **Arner**. Senator, let me first say that the returned-item process expedition of that has been through ANSI for some changes relative to positioning the endorsement and that type of thing, so we think we are making some progress, and that will enable us to return the item to the bank of deposit directly as opposed to the route it's taking now. That's what the objective of that effort has been, and it appears to be nearing fruition.

Senator **Dodd**. Do you have any timetable on that at all?

Mr. **Arner**. No. The standards are out for comment as I understand it.

Senator **Dodd**. Mr. Messina, the staff here has requested that the results you have on that survey that you just read be made a part of the record.

Mr. **Messina**. Certainly.

Senator **Dodd**. Well, we are about to get a new study, as you may have heard, from the Fed, and if after more than 2 years we see not even letters being written to CEO's, or any sort of communication that appears to suggest the implementation of policies that the 1979 task force recommended, I'm less than confident that this new study is going to be any more successful in terms of trying to improve a situation I think we all recognize can be improved.

Do you have any sense that the Fed takes this seriously?

Mr. **Arner**. Oh, I believe they do. I can't speak for the Fed, but it has been our contention from the beginning of that task force effort with the Fed that regulation would not serve in the best, I guess, efforts of trying to overcome the problem, and you've heard that time and time again.

Senator DODD. Yes. Everyone seems to understand that the very least we could hope for at this point is that there be consumer awareness of what the policies are. Whether or not we agree or disagree on the length or period of time for hold, at the very least we can expect that consumers be aware of what a particular institution's policies are. Those are the recommendations 2½ years ago and yet we can't even get a letter out of the Fed to the CEO's and banks suggesting that. How are we ever going to deal effectively if we can't even get a minimum on something we all agree upon. Regardless of whether or not we're sitting here or at the Fed or with the institutions, if the agency responsible for setting these policies cannot even manage to draft a letter suggesting a policy, how in the Lord's name are we ever going to expect much of a change?

Mr. ARNER. Senator, I would suggest that I think there is considerably more awareness in the commercial banking industry today, and there is more disclosure. It has come from within the industry. And I also would like to comment on the fact that you have a copy of our document which is made available to all customers that states our policy, and it says something about a maximum of 10 days to hold. I want to be sure, because I think sometimes we are inclined to treat this in a way that is somewhat misleading—although we have that policy in our rules and regulations and agreements, it does not mean we exercise that prerogative. In fact, I would suggest that it would be a rare occasion and if it happened 10 times in 1 day it would be significant. In our kind of an operation—and I think there are many, many banks that are being looked upon in terms of this progress.

Senator DODD. You were chairman of that task force in 1978 and early 1979. Are you going to be the new chairman of this one?

Mr. ARNER. They have not asked me and I'm not sure I will accept.

Senator DODD. Why?

Mr. ARNER. My duties have changed.

POSSIBLE CONGRESSIONAL ACTION

Senator DODD. Let me just tell you something. My experience, as limited as it may be, on Capitol Hill in the last 6 or 7 years is that it's a lot easier to regulate than deregulate, and what you're hearing today, I think, from two members of this committee who don't always share the same viewpoint on issues, is that there is a legitimate concern out there and that I think both of us—and I think we can speak for the vast majority of the people who serve on this committee—we would prefer that the industry police itself, discipline itself in this regard. There are no members up here salivating to regulate, but experience should teach you that in time—you have roughly 7 million consumers, whether they be small business people or individual accounts, who all of the sudden find that this is a massive problem for them, and you and I both know what happens—you'll end up with some form of regulation. In many cases it may not be the best thought out, but you will end up with congressional action, and we do that much more expeditiously than we end up deregulating, certainly.

So if I could leave you with anything today—and I should be careful about trying to express the views of the chairman, but I sense from his questions and his comments that while we don't anticipate anything in the legislative arena immediately that if something isn't done shortly in this area you can expect legislation to be introduced that will require certain activities in this regard.

I'll tell you, I'll do it if something isn't done. That's how seriously I consider it. As I said at the outset, there are a lot of other issues that enjoy a larger profile than this one today, but I think it's a very legitimate issue that affects not just individuals but industry and business across this country, and if we can't even get letters out from the Fed to suggest on a voluntary basis certain things we all understand would improve the situation, then I'll tell you, you're going to get some action up here, although I prefer that it was done the former way, on a voluntary basis than done through regulation.

But let me reiterate the concluding remarks of the chairman. I appreciate you being up here today and giving us a chance to air the issue anyway and certainly, as chairman of the task force in 1979, you did make some sound recommendations. I just regret that they weren't more effectively communicated to the institutions than they were, and my only request would be, whatever this new task force decides, whether it's the same thing that was decided in 1979 or not, that those recommendations and suggestions be made very strongly to the institutions through their representative organizations, that they will be saving themselves, I think, a tremendous problem that could occur if the Congress decides to take action and insisted upon legislation in this area.

Do any of you have any closing comments at all you want to make?

Mr. MESSINA. I can appreciate what the committee is trying to accomplish, and I think perhaps just bringing attention to bear on the issue might very well bring some efficiencies in this system and the end result that everyone is seeking.

Senator DODD. Thank you.

The committee will stand adjourned.

[Whereupon, at 12:25 p.m., the hearing was adjourned.]

[Additional material received for the record follows:]

1977 Consumer Survey Question on Delayed Funds Availability

The University of Michigan's Survey Research Center in 1977 conducted a study on consumer credit use and attitudes toward regulations affecting credit on behalf of the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency. A question contained in the study dealt with the practice of delayed funds availability. The question was as follows:

> Some banks have a policy making customers wait as long as four or more days before they allow the customers to withdraw money which was deposited in the form of checks. In the past few years how often has a policy like this caused you problems? Would you say you have had problems frequently, sometimes, hardly ever, or never?

Of the consumer questioned who maintained checking accounts, 87.6% responded "Never," 7.6% "hardly ever," 1.6% "frequently," and 3.3% "sometimes." The study did not contain additional questions that would have allowed determination as to the circumstances of the delays encountered by those who said they had encountered a delay.

EXTRACT FROM 1978 FRB SURVEY OF BANK PRACTICES

IV. 1. When a bank customer (i.e., an individual with an existing personal savings or checking account at the bank, deposits a check, is it bank policy or practice as communicated by the teller to temporarily delay the availability of those funds to the customer because of either the type of check, or the geographical located of the bank upon which it is drawn?

Response

Category of bank	Yes		No	
	Number	Per cent	Number	Per cent
All	322	38.1	524	61.9
Deposits (millions of dollars				
Less than 20	147	33.2	296	66.8
20 - 100	130	41.0	187	59.0
More than 100	45	52.3	41	47.7
Located				
Within SMSA	185	50.7	180	49.3
Outside SMSA	135	28.2	344	71.8
District				
1	21	61.8	13	38.2
2	28	68.3	13	31.7
3	12	48.0	13	52.0
4	10	27.0	27	73.0
5	34	52.3	31	47.7
6	61	58.7	43	41.3
7	40	23.3	132	76.7
8	34	42.0	47	58.0
9	14	16.3	72	83.7
10	29	30.2	67	69.8
11	26	33.3	52	66.7
12	13	48.1	14	51.9

NOTE

Bank responses to Question IV. 2. are selectively presented on the following six pages. That question asked banks to specify what delay in funds availability would be imposed when checks of various types, drawn on banks at various locations, were deposited in consumers' accounts. Banks were asked to specify their policy with respect to the following types of checks: personal, certified, cashier's or bank, traveler's, money order, private payroll, and governmental payroll. Banks were further requested to distinguish among checks drawn on same-city, out-of-city, out-of-county, and out-of-state banks.

Because of the volume of data collected on this one question, and because of the similarity of answers among a number of different categories, results have been reported for only four types of checks---personal, cashier's or bank, money order, and private payroll. In addition, the data is not broken down by Federal Reserve District.

The form of tabulation for the next six pages is different from the rest of the report in that data for each different category of bank is recorded on a separate page. A number of banks responded by giving a range of days that funds may be delayed (e.g., 5 - 15 days), rather than a specific number. Where this occurred, the period of delay for tabulation purposes was considered to be the high end of the range (e.g., 15 days).

IV. 2. If availability of funds is delayed, describe the bank's policy by type of check and location of bank upon which it is drawn.

A. All banks in survey

	Response											
	0 days		1 - 3 days		4 - 6 days		7 - 9 days		10 - 12 days		13 & more days	
Type of check location of payee bank	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal												
same - city	86	28.6	120	39.9	71	23.6	15	5.0	8	2.6	1	0.3
out-of-city	27	8.4	85	26.5	107	33.3	43	13.4	50	15.6	9	2.8
out-of-county	19	5.9	58	18.0	125	38.8	49	15.3	61	18.9	10	3.1
out-of-state	5	1.6	28	8.7	68	21.1	50	15.5	124	38.5	47	14.6
Cashier's or bank												
same - city	211	69.2	56	18.3	31	10.2	6	2.0	0	0	1	0.3
out-of-city	206	64.2	42	13.1	42	13.1	11	3.4	18	5.6	2	0.6
out-of-county	202	62.7	38	11.8	45	14.0	15	4.7	20	6.2	2	0.6
out-of-state	194	60.2	26	8.1	22	6.8	18	5.6	44	13.7	18	5.6
Money order												
same - city	204	66.9	60	19.7	33	10.8	6	2.0	2	0.6	0	0
out-of-city	202	63.1	43	13.4	39	12.2	14	4.4	20	6.3	2	0.6
out-of-county	198	61.7	37	11.5	44	13.7	18	5.6	22	6.9	2	0.6
out-of-state	192	59.8	24	7.5	25	7.8	17	5.3	46	14.3	17	5.3
Private payroll												
same - city	145	48.3	86	28.8	52	17.3	9	3.0	7	2.3	1	0.3
out-of-city	107	33.4	67	20.9	72	22.5	32	10.0	37	11.6	5	1.6
out-of-county	98	30.5	51	15.9	82	25.5	39	12.2	43	13.4	8	2.5
out-of-state	86	26.9	28	8.8	49	15.3	36	11.2	89	27.8	32	10.0

IV. 2. If availability of funds is delayed, describe the bank's policy by type of check and location of bank upon which it is drawn.

B. Bank with deposits less than $20 million

Type of check location of payee bank	Response											
	0 days		1 - 3 days		4 - 6 days		7 - 9 days		10 - 12 days		13 & more days	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal												
same - city	57	44.2	40	31.0	23	17.8	4	3.1	5	3.9	0	0
out-of-city	20	13.7	38	26.0	42	28.8	19	13.0	23	15.8	4	2.7
out-of-county	14	9.5	22	15.0	61	41.5	18	12.3	28	19.0	4	2.7
out-of-state	4	2.7	10	6.8	40	27.3	23	15.6	49	33.3	21	14.3
Cashier's or bank												
same - city	108	81.2	17	12.8	7	5.3	1	0.7	0	0	0	0
out-of-city	112	76.7	11	7.5	14	9.6	3	2.1	6	4.1	0	0
out-of-county	111	75.5	10	6.8	16	10.9	3	2.0	7	4.8	0	0
out-of-state	105	71.4	8	5.4	8	5.4	7	4.8	10	6.8	9	6.2
Money order												
same - city	103	77.4	21	15.8	8	6.0	0	0	1	0.8	0	0
out-of-city	107	73.8	14	9.7	13	9.0	4	2.8	7	4.7	0	0
out-of-county	105	71.9	12	8.2	17	11.6	4	2.8	8	5.5	0	0
out-of-state	101	69.2	6	4.1	13	8.9	6	4.1	11	7.5	9	6.2
Private payroll												
same - city	78	60.9	29	22.6	15	11.8	1	0.8	5	3.9	0	0
out-of-city	58	40.0	30	20.7	23	15.9	15	10.3	17	11.7	2	1.4
out-of-county	54	37.0	20	13.7	33	22.6	15	10.3	21	14.4	3	2.0
out-of-state	49	33.8	10	6.9	26	17.9	18	12.4	30	20.7	12	8.3

IV. 2. If availability of funds is delayed, describe the bank's policy by type of check and location of bank upon which it is drawn.

C. Banks with deposits of $20 - 100 million

	Response											
	0 days		1 - 3 days		4 - 6 days		7 - 9 days		10 - 12 days		13 & more days	
Type of check location of payee bank	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal												
same - city	27	21.2	56	44.1	35	27.6	6	4.7	2	1.6	1	0.8
out-of-city	7	5.4	35	26.9	48	36.9	16	12.3	20	15.4	4	3.1
out-of-county	5	3.8	27	20.8	46	35.4	22	16.9	25	19.2	5	3.8
out-of-state	1	0.8	14	10.8	21	16.2	21	16.2	55	42.2	18	13.8
Cashier's or bank												
same - city	84	66.1	24	18.9	15	11.8	3	2.4	0	0	1	0.8
out-of-city	77	59.2	23	17.7	16	12.3	5	3.8	8	6.2	1	0.8
out-of-county	74	56.9	21	16.2	18	13.8	7	5.4	9	6.9	1	0.8
out-of-state	73	56.1	14	10.8	10	7.7	8	6.2	20	15.4	5	3.8
Money order												
same - city	87	68.5	22	17.3	15	11.8	3	2.4	0	0	0	0
out-of-city	82	63.1	19	14.6	14	10.7	6	4.6	8	6.2	1	0.8
out-of-county	80	61.5	17	13.1	15	11.5	8	6.2	9	6.9	1	0.8
out-of-state	78	60.0	13	10.0	8	6.2	8	6.2	20	15.3	3	2.3
Private payroll												
same - city	55	43.3	39	30.7	27	21.9	4	3.1	1	0.8	1	0.8
out-of-city	39	30.0	29	22.3	34	26.2	11	8.5	15	11.5	2	1.5
out-of-county	34	26.2	25	19.1	34	26.2	17	13.1	16	12.3	4	3.1
out-of-state	27	20.9	15	11.5	17	13.1	15	11.5	44	33.8	12	9.2

IV. 2. If availability of funds is delayed, describe the bank's policy by type of check and location of bank upon which it is drawn.

D. Banks with deposits of more than $100 million

Type of check location of payee bank	Response											
	0 days		1 - 3 days		4 - 6 days		7 - 9 days		10 - 12 days		13 & more days	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal												
same - city	2	4.4	24	53.4	13	28.9	5	11.1	1	2.2	0	0
out-of-city	0	0	12	26.7	17	37.7	8	17.8	7	15.6	1	2.2
out-of-county	0	0	9	20.0	18	40.0	9	20.0	8	17.8	1	2.2
out-of-state	0	0	4	8.9	7	15.6	6	13.3	20	44.4	8	17.8
Cashier's or bank												
same - city	19	42.2	15	33.3	9	20.0	2	4.4	0	0	0	0
out-of-city	17	37.7	8	17.8	12	26.7	3	6.7	4	8.9	1	2.2
out-of-county	17	37.7	7	15.6	11	24.5	5	11.1	4	8.9	1	2.2
out-of-state	16	35.5	4	8.9	4	8.9	3	6.7	14	31.1	14	8.9
Money order												
same - city	14	31.1	17	37.7	10	22.2	3	6.7	1	2.2	0	0
out-of-city	13	28.9	10	22.2	12	26.7	4	8.9	5	11.1	1	2.2
out-of-county	13	28.9	8	17.8	12	26.7	6	13.3	5	11.1	1	2.2
out-of-state	13	28.9	5	11.1	4	8.9	3	6.7	15	33.3	5	11.1
Private payroll												
same - city	12	26.7	18	40.0	10	22.2	4	8.9	1	2.2	0	0
out-of-city	10	22.2	8	17.9	15	33.3	6	13.3	5	11.1	1	2.2
out-of-county	10	22.2	6	13.3	15	33.3	7	15.7	6	13.3	1	2.2
out-of-state	10	22.2	3	6.7	6	13.3	3	7.7	15	33.3	8	17.8

IV. 2. If availability of funds is delayed, describe the bank's policy by type of check and location of bank upon which it is drawn.

E. All banks located within an SMSA

Response

Type of check location of payee bank	0 days		1 - 3 days		4 - 6 days		7 - 9 days		10 - 12 days		13 & more days	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal												
same - city	27	15.0	75	41.7	62	34.4	11	6.1	5	2.8	0	0
out-of-city	9	4.9	49	26.4	65	35.1	26	14.2	30	16.2	6	3.2
out-of-county	5	3.2	33	17.9	72	38.9	32	17.3	35	18.9	7	3.8
out-of-state	1	0.5	15	8.1	30	16.3	27	14.6	79	42.7	33	17.8
Cashier's or bank												
same - city	110	61.1	38	21.1	27	15.0	5	2.8	0	0	0	0
out-of-city	107	57.8	26	14.1	31	16.8	9	4.9	11	5.9	1	0.5
out-of-county	105	56.8	22	11.9	31	16.8	13	7.0	13	7.0	1	0.5
out-of-state	101	54.7	14	7.6	13	7.0	11	5.9	33	17.8	13	7.0
Money order												
same - city	101	56.1	41	22.8	30	16.7	6	3.3	2	1.1	0	0
out-of-city	92	51.7	26	14.6	32	18.0	12	6.7	14	7.9	2	1.1
out-of-county	95	51.6	21	11.4	34	18.5	16	8.7	16	8.7	2	1.1
out-of-state	91	49.4	15	8.2	14	7.6	12	6.5	39	21.2	13	7.1
Private payroll												
same - city	62	34.6	57	31.8	47	26.4	9	5.0	4	2.2	0	0
out-of-city	50	27.2	37	20.1	49	26.6	20	10.9	24	13.0	4	2.2
out-of-county	47	25.5	28	15.2	51	27.7	25	13.6	27	14.7	6	3.3
out-of-state	42	22.8	15	8.2	26	14.1	16	8.7	61	33.2	24	13.0

IV. 2. If availability of funds is delayed, describe the bank's policy by type of check and location of bank upon which it is drawn.

F. All banks not located within an SMSA

Type of check location of payee bank	Response 0 days		1 - 3 days		4 - 6 days		7 - 9 days		10 - 12 days		13 & more days	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal												
same - city	104	86.0	13	10.7	2	1.7	1	0.8	0	0	1	0.8
out-of-city	104	79.4	12	9.2	8	6.1	2	1.5	4	3.0	1	0.8
out-of-county	103	78.0	12	9.1	10	7.6	2	1.5	4	3.0	1	0.8
out-of-state	100	75.8	7	5.3	11	8.3	4	3.0	8	6.1	2	1.5
Cashier's or bank												
same - city	99	80.5	18	14.6	4	3.3	1	0.8	0	0	1	0.8
out-of-city	97	72.4	16	11.9	11	8.2	2	1.5	7	5.2	1	0.8
out-of-county	95	70.4	16	11.8	14	10.4	2	1.5	7	5.2	1	0.7
out-of-state	91	67.4	12	8.9	9	6.7	7	5.2	11	8.1	5	3.7
Money order												
same - city	101	82.2	19	15.4	3	2.4	0	0	0	0	0	0
out-of-city	102	76.1	17	12.7	7	5.2	2	1.5	6	4.5	0	0
out-of-county	101	74.8	16	11.8	10	7.4	2	1.5	6	4.5	0	0
out-of-state	99	73.3	9	6.7	11	8.1	5	3.7	7	5.2	4	3.0
Private payroll												
same - city	81	68.1	29	24.4	5	4.2	0	0	3	2.5	1	0.8
out-of-city	55	41.0	30	22.4	23	17.2	12	9.0	13	9.7	1	0.7
out-of-county	49	36.3	23	17.0	31	23.0	14	10.4	16	11.8	2	1.5
out-of-state	42	31.3	13	9.7	23	17.2	20	14.9	28	20.9	8	6.0

IV. 3. If a "hold" is placed on funds, does teller inform customer of that fact as a matter of course, or only if the customer asks or indicates a desire to immediately use funds?

Response

Category of bank	As a matter of course		Only on request	
	Number	Per cent	Number	Per cent
All	243	75.5	79	24.5
Deposits (millions of dollars				
Less than 20	120	81.6	27	18.4
20 - 100	95	73.1	35	26.9
More than 100	28	62.2	17	37.8
Located				
Within SMSA	128	69.2	57	30.8
Outside SMSA	113	83.7	22	16.3
District				
1	6	28.6	15	71.4
2	8	28.6	20	71.4
3	9	75.0	3	25.0
4	10	100.0	0	0
5	29	85.3	5	14.7
6	54	88.5	7	11.5
7	26	65.0	14	35.0
8	31	91.2	3	8.8
9	12	85.7	2	14.3
10	26	89.7	3	10.3
11	22	84.6	4	15.4
12	10	76.9	3	23.1

IV. 4. **If the teller indicates that a "hold" is imposed, is there a bank official who is authorized to alter that policy in individual cases?**

Response

Category of bank	Yes		No	
	Number	Per cent	Number	Per cent
All	313	97.2	9	2.8
Deposits (millions of dollars)				
Less than 20	139	94.6	8	5.4
20 - 100	129	99.2	1	0.8
More than 100	45	100.0	0	0
Located				
Within SMSA	183	98.9	2	1.1
Outside SMSA	128	94.8	7	5.2
District				
1	20	95.2	1	4.8
2	28	100.0	0	0
3	11	91.7	1	8.3
4	10	100.0	0	0
5	32	94.1	2	5.9
6	61	100.0	0	0
7	38	95.0	2	5.0
8	32	94.1	2	5.9
9	14	100.0	0	0
10	29	100.0	0	0
11	25	96.2	1	3.8
12	13	100.0	0	0

IV. 5. If a bank official is authorized to alter the policy, what are the most important criteria used by that official in making a judgment to vary the policy?

In responding to this question banks were asked to consider five enumerated criteria and evaluate each one as being not important, somewhat important, or very important. Some banks also volunteered other criteria that their officers used. The criteria listed on the questionnaire were: length of time that an individual has been a bank customer, balance in account(s) that customer maintains, qualitative judgment about bank upon which check is drawn, type of check, and number of checks returned previously. Banks volunteered the following additional considerations: amount of check, customer's financial reputation and condition, nature of bank's relationship with the customer, and purpose of the check.

In view of the nature of banks' responses, separate tabulation of answers to this question would be both unwieldly and repetitive. As a whole, a substantial majority of banks responding (83%) considered the first two listed criteria (length of time as a customer, and balance in accounts) to be very important. The third criterion, a qualitative judgment about the bank upon which the check was drawn, was of no or limited use to 80% of the responders, while 94% considered the type of check presented to be either somewhat or very important. The final listed criterion, number of checks previously returned unpaid, was very important to 91% of the banks. Banks which described criteria other than those enumerated were almost unanimous in feeling that such additional considerations were also very important.

IV.6. How frequently does a bank official, at a customer's request, alter the policy expressed by the teller?

Response

Category of bank	Never		Infreqently		Frequently		Always
	No.	%	No.	%	No.	%	No.
All	7	2.2	275	88.1	30	9.7	0
Deposits (millions of dollars							
Less than 20	5	3.6	126	91.3	7	5.1	0
20 - 100	1	0.8	114	88.4	14	10.8	0
More than 100	1	2.2	35	77.8	9	20.0	0
Located							
Within SMSA	2	1.1	156	85.7	24	13.2	0
Outside SMSA	5	3.9	117	91.4	6	4.7	0
District							
1	0	0	18	90.0	2	10.0	0
2	0	0	22	78.6	6	21.4	0
3	0	0	10	90.9	1	9.1	0
4	0	0	10	100.0	0	0	0
5	1	3.1	28	87.5	3	8.4	0
6	0	0	55	90.2	6	9.8	0
7	1	2.6	32	84.2	5	13.2	0
8	1	3.2	28	90.3	2	6.5	0
9	1	7.1	13	92.9	0	0	0
10	1	3.4	26	89.7	2	6.9	0
11	1	4.0	23	92.0	1	4.0	0
12	1	7.7	10	76.9	2	15.4	0

POSITION PAPER: BAI DELAYED AVAILABILITY TASK FORCE ON RETURN ITEMS

NOVEMBER 1979

POSITION

The Bank Administration Institute Delayed Availability Task Force on Return Items has developed the following recommendations:

1. The task force feels that all financial institutions currently utilizing policies for advancing funds availability on personal accounts should base such polices on their experience in the collection and return of deposited items, and should not exceed the average normally expected collection and return period.

2. The task force encourages the Federal Reserve System to strictly enforce return notification rules and develop means for monitoring compliance. In order to initiate that effort, the task force recommends that the Federal Reserve help circulate the currently proposed publicity on the utilization of notification of large return items prepared by the Bank Administration Institute Return Item Notification Procedures Task Force.

3. The task force recommends that a change in the processing of return items be initiated with the cooperation of the Federal Reserve System. In order to improve the processing of return items the task force envisions a more direct routing of returns to the bank of first deposit utilizing the sorting and delivery

mechanisms of the Federal Reserve System. The ultimate aim of the proposal would be to automate, to the extent practicable, the return item process.

4. The task force finally recommends that the Uniform Commercial Code be improved in order to require financial institutions to utilize the most expeditious means of returning unpaid items.

The recommendations of the task force are the result of a considerable amount of discussion concerning both the policy and practice of return items and have been ranked in order of anticipated implementation capability.

BACKGROUND

In April of 1979, the Bank Administration Institute was asked by the Division of Federal Reserve Bank Operations of the Board of Governors of the Federal Reserve System to expand a currently operating Task Force on Return Item Notification Procedures in order to look at a consumer problem identified by the Federal Reserve. Based upon a number of consumer complaints, the Federal Reserve System had identified the banking practice of holding or delaying the funds availability of consumer deposits as requiring further study. The Federal Reserve System, in conjunction with the FDIC, and the Comptroller of the Currency, distributed a questionnaire in conjunction with bank examinations to obtain data on the current practices within the banking industry of funds availability for consumers' deposits. The results of the questionnaire were then compiled and the Federal Reserve, in conjunction with the American Bankers Association, convened a Delayed Availability Task Force to review the results of the questionnaire and to develop recommendations concerning the problem. The results of the deliberations of the Delayed Availability Task Force are included as an appendix to this report.

The Delayed Availability Task Force made a number of recommendations concerning both the practice and disclosure of delaying funds to consumer accounts. However, in their initial discussions, the Board of Governors Committee on Consumer Affairs felt that further work should be done to improve the causes of delayed funds, i.e., the inefficiencies of the return item system.

The Delayed Availability Task Force identified two significant problem areas in availability policies to the consumer. The first is that encountered by current customers of a financial institution when depositing items to an existing checking account. Many banks have established an across the board policy to "hold" the funds on consumer deposits, typically within certain dollar limits, in order to allow the deposited items sufficient time to be finally collected. The length of the "hold" varies from institution to institution but is typically implemented to allow for both collection time, as well as time for items to be returned in case of collectability problems.

The second problem identified by the task force was that experienced by new customers of a bank, especially those with large funds settlements from closing on property. New customers, whether moving into a new location or simply changing their banking relationships, often have needs for immediate funds, yet are unable to obtain immediate availability because of both identification and potential collectability problems for the institution. The task force made recommendations concerning studies to be undertaken in these areas in its report.

The Bank Administration Institute was asked to expand a currently functioning Task Force on Return Item Notification Procedures and continue its work to look into remedies for the availability problem through improvements in the return item process. At the same time, the American Bankers Association was asked by the Federal Reserve System to incorporate a task force aimed at developing a banking service for availability problems encountered by new customers of a bank.

The expanded BAI Task Force on Return Items examined the report of the Delayed Availability Task Force, as well as the current deliberations of the Return Notification Procedures Task Force. The charter of this expanded task force was to be the examination of "delayed availability" as it affects the currently established banking customer.

In its discussions, the task force felt that extending funds availability based upon collectability was a banking practice that was in the best interests of both the financial institution and its customers. The length of any hold on a consumer's deposited funds was found to be in two parts. First, the check is given time to reach the payor bank through the outward bound side of the check collection system. This is the same practice applied to commercial customers of the bank, who are allowed to utilize only those funds that have been collected, i.e., funds that have ultimately reached the payor bank for final payment.

In addition, availability polices can be implemented as part of the pricing strategy of the bank in order to maintain investable collected balances, while minimizing direct costs to the consumer for checking account services. When used in this manner, the length of the availability hold would be based as much on required balances as on collection time.

Financial institutions have also further extended the availability of consumer funds in order to account for items that may not be paid when finally presented to the payor bank. The return item portion of the check collection system takes considerably longer and is currently not as automated as the outward bound portion of the system. As a result, the time delay for receiving notification of final payment is much longer through the return item process than the time it takes for initial presentment of the item. As a result both of fraudulent activities and the irresponsible financial actions of a few customers, the practice of delaying availability in order for a bank to be as certain as possible that the item has been finally and irrevocably collected has been continued.

The task force has felt that the outward bound portion of the check collection system has received the bulk of the attention of the operations departments of the banking industry, and is probably automated to the extent that major improvements in the timing of the initial presentment of items are unlikely. However, the return item process is currently not automated and certainly not fool-proof and is the proper focus of the task force in order to bring about improvements in availability.

PROPOSAL

The task force thoroughly reviewed and discussed the return item process in developing a four point recommendation plan. The position of the task force was briefly discussed in the initial section of this paper. The following discussion further explains the reasons and strategies behind each of the recommendations of the task force. A group of ancillary recommendations developed during the task force deliberations, but not specifically addressing funds availability are included as an appendix to this report and are commended to the industry to improve customer service.

Based upon the discussions of the Return Item Task Force, the following recommendations were developed:

1. The task force feels that all financial institutions currently utilizing consumer availability policies base their policies on actual experience in the collection and return of deposited items. If a bank does not currently have an availability policy for consumer accounts, the task force does not recommend that a bank develop such a policy. The task force endorses the three following recommendations of the Delayed Availability Task Force; "(a) That the Board of Governors of the Federal Reserve System recommend that each bank have a written policy on delayed funds availability that is consistent with task force recommendations; (b) That the Board of Governors of the Federal Reserve System not attempt to define specific times associated with the length of allowable delay. Rather, delayed funds availability imposed by a bank should be defensible on the basis of that banks check collection records,

and, at a maximum, should not exceed the normally expected clearing and return period; (c) That the Board of Governors of the Federal Reserve System consider requiring that each bank have a written policy on delayed funds availability and disclose the provisions of that policy to each affected customer."

The task force believes that banks of first deposit should be encouraged to utilize their most recent experiences in the collection and return of items in order to establish availabilities for their customers. Each bank is also encouraged to develop a written policy concerning availability and make it generally available to customers either when opening new accounts or when they may be affected by depositing large items drawn on other banks. The bank policy should be subject to periodic internal review and examination by the appropriate regulatory authorities.

2. The task force encourages the Federal Reserve System to more strictly enforce the return item notification rules. The task force felt that improved notification was an initial positive step towards improving the entire return item process and was something that could be implemented fairly quickly without requiring major technological changes that would tend to restrict improvements only to major banks.

In order to enforce existing notification rules for large dollar return items, the task force is requesting the Federal Reserve System, all Clearinghouse Associations and major direct send correspondent banks to monitor banks' compliance with the rules. Periodic reports should be developed on each bank's performance and sent to the appropriate department manager, as well as the senior operating officer and chief executive officer of the bank. The reports would not, obviously, ensure full compliance, but the task force feels that they would provide sufficient incentive through senior management involvement. Many clearinghouses report fines to senior management and some Federal Reserve Banks similarly report reject rates, and both have been very successful in bringing corrective action.

An additional recommendation that should assist in the compliance with notification rules would be to insist that banks' of first deposit desiring notice on large items being dishonored comply with the endorsement standard currently being promulgated. The endorsement standard is designed to make the endorsements of the bank of first deposit and the first high speed processing bank legible by assigning areas on the reverse of the check for those imprints. If a bank wishes to receive return item notification they must take the trouble to comply with the standard. It is also envisioned that, as the standard gains wider acceptance, the report of notification compliance mentioned above would indicate the percent of notifications received on items complying with the endorsement standard and the percent received on return items not in compliance.

Additional pressure could be exerted on banks not wiring on items that follow the standardized endorsement.

The task force further recommends that the Federal Reserve reinstate the policy of notifying on return items, even if notice was not received from the returning banks, on those items that are in compliance with the endorsement standard. The banks that follow the standarized endorsement will be indicating a desire to receive notification on return items. The Federal Reserve should provide that notification, and then bring pressure on the dishonoring bank if they did not originate the notice.

Additionally, the task force endorses the currently proposed publicity on the utilization of wire notification on large return items prepared by the Bank Administration Institute Return Item Notification Procedures Task Force. This task force has developed a report on the utilization of wire notification procedures.

One of the methods of publicity contemplated on wire notification procedures was to place an article on the results of the task force deliberations in the Magazine of Bank Administration and to have that article reprinted by the Federal Reserve System and delivered to every bank in the country along with a letter from the president of the local Federal Reserve Bank encouraging banks to read and adhere to wire notification policies. The task force encourages the Federal Reserve to help implement this method of publicity and, at a minimum, send a review of the wire notification rules as well as the compliance report, if adopted, to every bank and clearinghouse association in the country.

3. Return items have become a major banking industry problem. Even though the volumes have grown, processing has not kept pace, is still essentially manual, and requires highly skilled clerical staff to decipher often unreadable endorsements. In addition, the delivery of returns to each previous endorser is typically done through the mail, with all the inherent delays. The task force has developed an alternative return item processing scheme that addresses both of these problems.

The task force recommends that return items be sent to the bank of first deposit directly through the sorting and delivery mechanisms of the Federal Reserve System. All previous attempts to improve return item processing have hinged on the standardization of the placement of endorsements. With the upcoming resolution of the endorsement problem through the ANSI committee the task force feels that carrier envelopes could become a viable solution to the processing of return items. It was noted that the Canadian banks are currently using carrier envelopes to handle return items with some measure of success.

As envisioned by the task force, a carrier envelope would be distinctively preprinted for returns and have the check off boxes to indicate the reason for return. The envelope would be encoded by the returning bank with the routing number of the bank of first deposit, or the first high speed processing bank, as well as the amount of the item. These documents would be processed amd settled separately from regular cash items.

All of the return item carrier envelopes for items not being returned directly through the local clearinghouse would be sent to the local Federal Reserve Bank office. The Fed would high speed sort the returns by Fed office and send them via the consolidated shipment to be sorted and delivered to the bank of first deposit in the next Fed delivery. Return items remaining in the local Fed zone would also be sorted by bank of first deposit and delivered in the next Fed courier run.

This method of processing out-of-district returns would allow high speed processing after the items have initially been encoded, would eliminate numerous error-prone manual handlings and minimize transportation delays and uncertainties. The banking industry would be able to rely on the collectability of deposited items, and should be notified sooner if an item has been dishonored.

The task force is well aware that the endorsement standards will not be implemented overnight, nor will they be strictly enforceable, unless the Federal Reserve adopts a policy to that effect. However, the same system described above can be put to immediate use without carrier envelopes, and be almost as effective. Manual sorting would take more time, but the number of institutions handling the items would be decreased. In addition, the improvements in transportation could be immediately realized.

While realizing that legal problems and timing considerations need to be resolved, the Task Force urges the banking industry and the Federal Reserve System to begin preliminary discussions into not only the feasibility of the recommendation, but also the implementation of a pilot project to test the system and work out areas of concern. The industry should not wait until endorsement standards are fully implemented before working on returns, because working the problems out of the manual system, on a small scale, will allow a faster and more successful implementation of an automated process.

4. The task force finally recommends that the Uniform Commercial Code be improved in order to require financial institutions to utilize the most expeditious means of returning unpaid items. The Code as currently written allows a financial institution to return items by merely dropping them in the mail as late as midnight of the day following receipt. Due to the nature of the postal system, delays in the physical return of items has become one of the biggest problems within the industry today. It has resulted in the problem of delayed availability currently being addressed by this task force, and has resulted in losses not only to financial institutions, but to their customers as well. The task force felt that the UCC ought to be examined in order to tighten wire notification rules as well as the methods of returning items. One problem with the UCC that needs to be resolved is the differences between Articles 3 and 4 that cause problems in

the return item process. Article 3 seems to indicate that wire or telephonic notification is sufficient, but Article 4, which takes precedence over Article 3, indicates that written notification, i.e., the physical return of the item, is the only allowable method for charging items back to the depositing bank. These problems need to be resolved in order to allow further improvements in the return item process, and utilization of technological changes that have come about and are sure to come about in the future.

CONCLUSION

The recommendations of the task force, at this time, are the result of a considerable amount of discussion concerning both the policy and practice of return items. The recommendations have been ranked in order of anticipated implementation capability. It was felt that the recommended policy decisions and the publicity campaign on wire notification could be implemented fairly quickly by the Federal Reserve and commercial banks.

However, revamping of the return item process needs to be begun as soon as possible, but, as experience has shown, will take a considerable amount of time and effort to bring to a decision and implement. Finally the review and proposed restructure of the Uniform Commercial Code, may be a never ending chore. However, the fact that a committee is in place reviewing Articles 3,4,and 8 of the Code leads us to hope that some improvements can be made within a reasonable time period.

Appendix I - Ancillary recommendations

All banks are encouraged to improve controls and policies covering customer accounts. The poor control for opening new accounts as well as for screening existing accounts for irresponsible financial behavior helps to contribbute to the return items problems experienced by the industry, which in turn causes funds to be delayed to responsible customers.

Depositor banks are encouraged to utilize alternative methods of collection and service for existing customers when delaying availability would cause those customers inconvenience. Two of the many alternatives for improvements in service would be to encourage the utilization of collection routes for cash items, or to offer the customer the alternative of calling the payor bank to determine final payment if the funds need to be more readily available. The task force does not necessarily endorse an increase in items being sent for collection. However, providing alternative services to a customer should be part of each banks efforts to provide the best personal service possible and advising the customer, in advance, of the options should improve customer relations.

Providing the customer with the alternative of sending items for collection allows both the bank and the customer to be certain that the item has been finally paid and that there is no possibility of return. The collection process, however, can take longer than a customer may wish to wait for final payment. In those cases, the bank could provide the customer the option of calling the payor bank to determine if final payment has been made. Based upon current clearing arrangements and allowing for payment of the item, the bank could call the payor bank in "X" days to determine if the item has been finally paid and then allow the customer to withdraw the funds. The task force is not suggesting that these services be offered without charge, but felt that a reasonable charge imposed for collection items and for the time for telephone calls would be acceptable to a customer in order to improve availability and certainty of final payment.

A related problem that was brought to the attention of the task force was that some banks routinely delay the availability on payroll checks for existing customers. This is a related problem to delaying availability on occasional high dollar items deposited, but becomes a extreme inconvenience to a customer when done to routine deposits utilized for living expenses. A survey done by the Federal Reserve System, Federal Deposit Insurance Corporation and the Comptroller of the Currency discovered that 40% of the responding banks routinely put a hold on payroll checks. The task force felt that this was a two-pronged problem.

First, banks are apparently not basing policies for availability upon the experiences and financial responsibility of existing accounts. The task force felt that any account that had been depositing payroll checks for a minimum of three months, could be examined for financal responsibility, and availability could be advanced to any customer meeting the bank's criteria. It was also felt that banks could review credit worthiness of the employer issuing payroll checks in order to determine the acceptability of payroll items for more immediate availability.

The second aspect of the problem is a failure by the customer's employer to recognize its responsibilities to its employees for making payroll funds immediately available. A number of remedies exist for employers to improve the availability of payroll items such as direct deposit of payrolls through the ACH, compensating balances at cooperating financial institutions for both check cashing and payroll check availability, as well as the possibility of drawing checks on local bank relationships in order to improve the availability of funds for its employees.

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